MODERN COMMERCIAL POLICY

A Study in Technique

BY

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opinion will have to play an active, vigilant and effective role in selecting and guiding their representatives in securing stable world peace and economic and political security for all and seeing that they do not sow seeds of another world war as they did at Versailles These representatives must be men of foresight and understanding A successful warrior is not necessarily a great statesman The constitution of the Peace Conference and the evolution of the future World Order will require very careful thought The public, therefore, has a heavy burden to shoulder and serious responsibility to discharge The economist will also have to play an important role in this task of post-war economic reconstruction

A word of explanation may be added here This work was completed before the outbreak of the present War The economic developments since then have been many and of far-reaching character Therefore wherever possible and necessary, important developments have been noted, but the fact remains that there has been no material change in the technique of Commercial Policy The War has only helped the extension of the rigid and restrictionist type of commercial policy which Nazi Germany had adopted as early as 1934 and perfected it thereafter In fact since 1934, German economic policy has been almost on war basis Great Britain also built up an armoury of restrictionist measures and resorted to blockade against Germany which had already anticipated the British move and had regulated its commercial policy accordingly Despite these tactical changes and adjustments the essentials of the Technique of Modern Commercial Policy have however, remained the same

War-time developments have immensely increased the necessity for a rational commercial policy in any scheme of international economic reconstruction and efficient utilisation of world economic resources Full and free scope for the expansion of world trade is essential to provide a durable basis for world peace Restrictions on

international trade must be removed As President Roosevelt has recently said "we must make sure that no effort will be spared to place international commerce on a basis of fair dealing equality of treatment and mutual benefit In no other way can it serve the function of promoting rather than retarding peaceful relations among nations and economic well-being of all '

The present work is a critical analysis of the technique of Modern Commercial Policy and contains suggestions for post-war reconstruction It is both critical and constructive This work is therefore addressed as much to the general public as to students of economics, who will have to play an important role in securing a just and stable economic order

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INTRODUCTION

Importance of the Subject:

A study of the technique of modern commercial policy needs no apology During the post-war period, particularly since the depression the technique of commercial policy has recorded remarkable changes The introduction of quotas, exchange controls, clearing agreements, import monopolies, milling regulations, etc, represents a radical depaturre from the conventional technique These measures have restricted the flow of international trade and affected adversely the standard of life of the people in most countries International relations have been strained, leading to economic and political instability This technique led to suspicion and misunderstanding between nations, which in turn, have further strengthened the restrictionist policies The whole situation has, thus, become extremely grave The economic implications of these new measures should, therefore, be studied and their dangers brought home to the general public, for, a well-informed public opinion alone can restore sanity in modern commercial policy

Special Significance of this Study to India:

A critical analysis of this technique is of special significance to an industrially backward country like India, where the state has so far failed to formulate a definite economic policy in keeping with the requirements of the people The present economic policy of the Government of India is a medley of incongruities It is a curious mixture of *laissez faire*, on the one hand, and haphazard and half-hearted protectionism, on the other The dangerous principle of discrimination, in the form of Imperial Preference, has become an integral part of our tariff policy

Import quotas have also crept in In commercial treaties, there is hardly any definite thought out policy of negotiating a net-work of br commercial treaties in order to find suitable markets for our exports What India needs is a carefully thought out commercial policy able to protect her national interests against the aggressive economic policies pursued by foreign countries and at the same time contribute her quota towards the improvement of international economic relations A fuller understanding of the technique of modern commercial policy is essential for the formulation of a national commercial policy which would satisfy the reasonable economic requirements of the nationals of the country, and encourage complementary exchange between countries If economic history is any guide it must be admitted that the growth of stable economic internationalism rests upon healthy nationalism The right of industrially backward countries to develop their economic resources must be recognised and adequate financial assistance extended to them The industrially advanced countries should take these new competitors in good grace and discard the element of economic self-sufficiency from their commercial policy

Available Literature on the Subject

It is in the fitness of things that the literature on the technique of modern commercial policy has been growing rapidly We shall refer here only to a few important works The publications of the League of Nations and the International Chamber of Commerce are of special interest in this connection For example the Annual World Economic Survey and the special memoranda prepared for the World Economic Conference are very useful Reports on Exchange Control and Clearing Agreements are equally illuminating The volumes in the Treaty Series published by the League of Nations are useful so far as the texts of the treaties are concerned, though the texts of the commercial treaties can also be found in the Board of Trade Journal Prof Bertil Ohlin's Report on International Economic Reconstruction and Memoranda attached thereto

are valuable as primary sources of information, and others as important contributions to specific aspects of modern commercial policy It is, however, not possible even for a good student of Economics to wade through this mass of literature in order to have a correct view of modern commercial policy A systematic study of the recent developments in commercial policy which may undertake to examine the theoretical aspects of the same, on the one hand and analyse the facts on the other would provide a comprehensive review of the entire problem, which would prove useful not only to the economist but also to the statesman

An ambitious piece of research work of this nature can be successfully undertaken by experts and organised by the League of Nations The different governments may be asked to lend their co-operation by giving the necessary information and in other ways It is only by some such comprehensive effort that a well co-ordinated study can be made which will be useful to all those interested in the problem

In view of this, it is difficult for an individual student to attempt to fill the gap In spite of this, a modest effort has been made in this work as an introduction to this larger need Because of obvious limitations of work by an individual student attention has been directed only to the more important features of the problem

Scope of this Study:

In the first chapter, we have given an outline of the evolution of commercial policy, for, the implications of this new technique cannot be adequately understood except in relation to its past A proper historical perspective alone can enable us to understand the economic significance of some of the important changes that have taken place in recent years In the second chapter we have tried to state briefly the more important economic problems of the period

of the Great Depression, and the nature of the new instruments of commercial policy These chapters provide a general background for a detailed study of the economic implications of the new commercial policy

For the purposes of detailed study, we have selected tariff bargaining methods, quotas exchange control including clearing and compensation agreements, and the Most-Favoured-Nation Clause Four chapters have been devoted to a critical analysis of the new technique of commercial policy Each important instrument of commercial policy has been assigned a chapter, and its economic implications have been examined. The dangerous consequences of these restrictionist measures have been pointed out and suggestions made for suitable improvements

To make our study of the technique more realistic, we have reviewed the recent commercial policy of the United States of America, the United Kingdom and India Besides, a special chapter has been devoted to a study of the Ottawa Scheme of Imperial Preference In this way, we have been able to draw upon the varied experience of different countries with widely different outlook in our review of the application of the new technique in practice For example, the dominating influence of British commercial policy on international trade has been noticed, and the dangers inherent in that policy, including the Ottawa Scheme of preferences, pointed out At the same time, a critical analysis of the trade agreements programme of the United States shows the part which a sober commercial policy can play, even in the most difficult and complicated of international economic conditions, in improving commercial relations and reducing trade barriers The review of Indian commercial policy, or rather the lack of a proper commercial policy, shows the defenceless position of a backward country under present conditions The need for a definite and carefully thought out commercial policy is particularly great for an industrially backward country to protect her economic system against the aggressive economic nationalism of other countries We have shown that

such a strong policy can play a useful part in improving international economic relations

In the concluding chapter we have made suitable suggestions for removing the discriminatory and aggressive character of modern commercial policy The present economic and political conditions in the world are obviously intriguing and the complications in modern commercial policy have unfortunately a tendency to increase The fear of war and the consequent economic and political insecurity are largely responsible for the growing restrictions on international trade A mutual understanding between nations can alone improve the present chaotic situation and pave the way for any sound scheme of international economic rehabilitation

We have seen that the technique of commercial policy is extremely complicated Besides it is subject to dynamic forces Each important commercial treaty as it finally emerges from the hands of those responsible for negotiation is usually quite distinct from the rest of its kind Each treaty serves the growing needs of contracting countries at a particular time In a dynamic society economic and political requirement which a commercial treaty is intended to serve change rapidly and affect both the contents and form of the treaty though changes in form are less frequent and marked Numerous interests often conflicting have to be taken into consideration and carefully weighed For instance the schedules containing tariff duties usually attached to commercial treaties, are based on elaborate statistical studies undertaken by official and semi official bodies in both the contracting countries The incidence of each duty has to be studied in detail and conflicting claims reconciled Thus a tariff schedule well adapted to the growing needs of modern society is the product of a long process of evolution The same is true of other features of commercial treaties The task of a student of modern commercial policy is therefore both difficult and delicate The data to be studied are extensive and ever changing Generalisations are therefore risky and apt to become unrealistic with changes in economic conditions

CHAPTER I

EVOLUTION OF COMMERCIAL POLICY

PROTECTION has played a prominent part in relieving the birth pangs of the modern industrialism Almost every industrialised country has had to protect its industries against foreign competition, for a temporary period, so as to enable them to consolidate their position Rationally applied, protection enables the most efficient utilisation of the natural resources, human skill and aptitudes, and maximises international trade and commerce But the application of protection must essentially be moderate,[1] cautious and temporary, lest it should create vested interests, breed inefficiency and become permanent The evolution of modern commercial policy clearly shows the advantages of the protectionist policy as well as its dangers and drawbacks In short, at a certain stage in the industrial development of a country protection must assume the imporance of a tenet In the present chapter, therefore, an attempt will be made to trace, in brief, the evolution of modern commercial policy This historical study will show us the technique of commercial policy pursued in the past and its effects on the growth of trade and industries Further, it would be a guide in re-shaping our commercial policy, so as to improve the international economic relations and stimulate the growth of world trade

BRITISH COMMERCIAL POLICY

Protection in aid of industrialisation.—British commercial policy has been aptly characterised as one of definite and carefully thought-out protectionism since 1651 The Industrial revolutions introduced marked changes in her economic and industrial organisation and sounded a death-

knell of the primitive methods of production on which the industrial system of the world till then depended No wonder, therefore, that within forty years from the inception of the industrial revolution in England, British industries recorded a remarkable growth But in this process of industrial expansion, protectionist policy played a very important part, it enabled the British industries to consolidate their position against foreign competition During this period protective tariff was used essentially as an instrument of self-defence, the imports were almost entirely excluded After some time improved technique of production enabled the British industries to turn out articles of high quality at very cheap prices, with which no other country could successfully compete Therefore Britain soon became the workshop of the world By this time protection had achieved its objective From the structure of British industries in 1860 it was evident that protectionist policy could be completely discarded to enable the industries to draw their raw materials freely from foreign countries and find markets abroad for their finished products

Free Trade Ideology.—The evolution of this free trade ideology in Britain, was, however, gradual and in keeping with the requirements of British industries and commerce Theoretical generalisations of Economic Science were suitably moulded to suit the practical problems of economic policy During the first half of the nineteenth century import duties, prohibitions bounties, shipping privileges, etc , were gradually abolished

Huskisson's Reforms.—Credit goes to Huskisson for having attempted for the first time to reform the commercial policy in the direction of relaxing restrictions on trade He simplified the customs laws, which had worked considerable hardship on traders Further, in 1824 he reduced duties on certain raw materials, imported for the British industries, notably coal, wool and silk The restrictions on exports were also abolished

Another interesting feature of these reforms is that the system of bounties on exports was considerably discouraged The bounties for the encouragement of whale fishery and exported silks were allowed to lapse in 1824 Corn bounty had fallen into disuse Linen bounties were also discouraged But the sugar-bounty survived the attacks of the critics, and cost about £100 000 during 1828 [1] In short, bounties were substantially curtailed and lost much of their importance

The system of imperial preference, however, continued, notwithstanding the most severe criticism of eminent economists Parnell calculated that the East India Company's monopoly of tea, which was of the nature of a much exaggerated imperial preference, made the price of tea, exclusive of duty, double of what it was at New York and Hamburg and imposed a tax of at least £2 million a year in the form of higher prices, that the preferential sugar-duties, by keeping out cheap foreign and East Indian sugar, were a tax on the public of at least £1 5 million a year, and that the monopoly of timber trade enjoyed by the shipowners and Canadian merchants cost more than a million pounds a year [2] To these must be added coffee, hides and textile raw materials as the outstanding examples of preference Substantial preferences were also granted on several other raw articles like pig iron, iron bars, sperm oil, tallow, gum, box-wood, soap, resin etc The colonies and the overseas possessions were, in turn, required to give a preferential treatment to the produce and manufactures of the U K The result was that the mother-country still practically enjoyed all the advantages of the old monopoly with respect to supplying the colonies with her articles It was the heavy taxation on the alternative foreign articles, rather than the preference *per se*, which drew the fire of the economists [3]

Huskisson's Navigation Act of 1825 codified the law relating to shipping but kept all the old principles intact

There was still a list of goods, the produce of Europe, which might not be imported into the U K, to be used therein, save in British ships or in the ships of the country of which the goods were the produce, or in the ships of the country from which the goods were imported Thus, conditions were liberalised in the interests of the British and particularly the entrepot trade The coasting traffic and the whole carrying trade between Britain and her colonies were still reserved for British ships "All intercourse between the mother country and the colonies, whether direct or circuitous," said Huskisson, while introducing the Bill "and all intercourse of colonies with each other, will be considered as coasting trade to be reversed entirely and absolutely to ourselves "[1]

Thus, taken as a whole, Huskisson's Reforms did make some breaches in the protective system, but did not alter the system in any essentials For instance, instead of being prohibited, under the reformed system French silks paid 30 per cent *ad valorem* but the new duty proved strong enough to keep most of the French silks out Similarly, the consolidation of all duties on cotton manufacturers at a uniform level of 10 per cent *ad valorem* had no perceptible effect upon the imports Same was the case with the reductions in duties on wollens, glass, gloves, linen, etc The final omnibus clause of the budget of 1825 which fixed the duty on all manufacturers, specially dealt with, at 20 per cent, shows the essential conservatism of the reforms In view of Britain's industrial leadership the general level of 20 per cent tariff protection was more than enough to close her port-markets to most foreign manufactures [2]

That the imports pay for the exports is an elementary principle of economics The free traders therefore, rightly argued that the fiscal policy of the U K, which deliberately checked imports, checked also the growth of industries which manufactured for export The British

1 Quoted by Clapham p 312
2 Supra p 326

industries, due to their technical efficiency, had grown substantially but the expansion would have been still more rapid if Britain had permitted a free scope to imports Further, the British protectionist policy gave added strength to the protectionists in the European countries, particularly in France and Russia The German market was still open for the British goods, but it was almost stagnant America adopted a severe protective system with an interlude of free trade, but provided a very valuable market for British manufactures India and China in the East also provided growing markets In short, notwithstanding the reforms of 1824-25 the British commercial policy continued to be severely protectionist According to Mr Clapham "most of the customs duties on manufactures did not yield revenue and were not intended to yield revenue They were frankly protective"[1] Still in 1827, the total net revenue from customs and excise was about 139 million, whereas the net revenue from all other forms of taxation was 113 million only Import duties were levied on foodstuffs, like corn, bacon, butter, cheese, lard, etc Raw materials were also taxed and included 'cotton wool', raw and thrown silk, wool, flax, hemp, etc Excise duties were levied on glass, paper printed calicos and muslins

In 1833 restrictions were further relaxed On about 58 articles duties were completely abolished, and substantial reductions were made on about 700 articles This was another breach in the protective system, but it did not mark any radical change

Role of Peel as Tariff Reformer.—To Peel goes the credit of having effected a radical departure from the traditional protectionist policy A general customs revision was made in 1842 whereby all prohibitory duties were removed and substantial reductions were introduced on a large number of articles of import, especially foodstuffs and raw materials In a total of more than 1,150 items in the list of

dutiable goods, 150 were subjected to modification A more liberal sliding scale of duties mitigated the severity of the Corn Laws Further remissions in duties were effected in 1844, and in 1845 about 430 petty items of tariff were abolished In 1846 an Act was passed whereby the Corn Laws were to be abolished entirely by the 1st of February, 1849 Duties were also either abolished or reduced on about 150 raw materials and foodstuffs by the same Act The repeal of the Corn Laws sounded the death knell of protectionism in England But these tariff reforms cost Peel his office

Tariff Reforms of Gladstone—The reforms of Huskisson and Peel drew the sting out of the British protective system and facilitated the task of the future reformers Even then the path of a tariff reformer was not so smooth as it might seem to be at the first sight Gladstone had an uphill task In 1853 Gladstone succeeded in removing duties on about 120 articles and in reducing them on 140 others In 1860 he negotiated a commercial treaty with France and reduced the total number of taxed imports to 48 Thus, by 1860 England became a full-fledged free trader By this time the British exports reached an annual value of £165 million (i.e more than 30 per cent of the total world trade) and the tonnage of British shipping was 5 7 million tons, which represented 34 6 per cent of the world total The remaining duties were slowly reduced—hops duty in 1862 timber duty in 1869 and sugar duty in 1875 so that the number of taxed articles came down to about 20 and remained so until the outbreak of the War

Britain adopted free trade not in deference to any abstract theory, or as an outcome of any popular propaganda, but because the logic of the whole course of the country's economic development gradually led to it The British industries, having sufficiently grown, felt the necessity of ample and cheap supply of raw materials and an open market for their manufactured articles Under the protective system the European continent could not

absorb the desired quantity of British goods, since duties were so high as to offset all the advantages of exchange The abolition of import duties by England, by facilitating imports from the continental Europe, increased the volume of both export and import trade with foreign countries The continental countries, by increasing their exports to England, were able to purchase a correspondingly larger amount of British manufactures It does not, therefore come to us as a surprise to find that within five years after the repeal of the Corn Laws the British exports rose from fifty to one hundred million pounds Between 1855 and 1900, the British exports rose from £116 million to £183 million and the imports from £146 million to £460 million In 1913 the value of the British exports rose to £525 million and that of the imports to about £769 million. During this period Britain specialised in manufacturing industries, and imported raw materials and foodstuffs

The rapid progress recorded by the British industries under tariff protection afforded a striking example for other countries to emulate Some of the more important countries in Europe, therefore reorganised their industries under a tariff wall during the last quarter of the nineteenth century The most obvious result of this change was that these countries not only reduced their imports of the British manufactures but commenced serious competition with the British goods in other foreign markets Hence, before the end of the nineteenth century the need for tariff reform was felt in Britain Being a free trader, Britain had hardly any concession to offer by way of commercial reciprocity Further, at this stage, to the claim of tariff reform was added the principle of imperial preference by Joseph Chamberlain He believed that the introduction of a general customs tariff with an average duty of 10 per cent ad valorem on foreign manufactured goods, duties on grain, flour, dairy produce, and meat, imported from foreign countries, plus a British preferential tariff for the Empire products would permit the organi-

sation of an independent Imperial Economic Unit Such a policy would also supply the means of negotiation for a more favourable treatment of the British goods in the foreign countries

The adoption of imperial preference at this time would have marked a radical change in British commercial policy The British Government, fortunately, unequivocally declared its intention in favour of free trade in the interest of the nation as a whole by negotiating the Cobden Treaty with France in 1860 If the policy of imperial preference was accepted it would have involved the imposition by Great Britain of import duties on foreign foodstuffs which the public opinion in England strongly disliked So also the scheme would have necessitated the levy of import duties on the raw materials required by the British industries, because the Empire supplies could not adequately meet the requirements Above all, the Empire could not absorb the rapidly increasing output of the British industries, which had to depend upon the foreign markets In short, the policy of imperial preference was not in the best interests of the British people at the time Therefore, Joseph Chamberlain, in his appeal to the country on the question of tariff reform in 1906, was overwhelmingly defeated Similar results followed after the General Election of 1910 But the supporters of the protectionist revival remained undaunted and continued their campaign unabated till the declaration of the Great War

The Great War demonstrated the military danger and drawbacks of free trade and prepared the most fertile soil in which the seeds of economic self-sufficiency germinated on an extensive scale for the first time in the modern economic history During the hostilities, the belligerent countries suffered great hardships due to the shortage of the supplies of essential foreign materials Britain, for instance, experienced considerable difficulty due to the scarcity of essential foodstuffs and raw materials The protectionists, in support of their case, attributed the

hardships resulting from the scarcity of raw materials and foodstuffs to the policy of free trade, and emphasised the necessity of fostering key industries within the borders of the U K and to so strengthen the economic ties between the different parts of the Empire as to create a single self-supporting Imperial Economic Unit

The measures taken during the War marked, in effect, a return to protectionism in Britain The Finance Act of 1915 imposed duties of 33 per cent on clocks watches and component parts, cinematographic films, motor cars commercial vehicles, the accessories and the component parts, tyres, musical instruments and the accessories These duties, known as McKenna Duties, were intended to restrict the luxury imports The following year the Board of Trade set up the Department of Import Restrictions with powers to regulate imports But the measures taken during the war cannot be taken to effect any permanent departure from the policy pursued during the normal period, they were essentially emergency measures

It must, however, be admitted that the war effected marked changes in the economic outlook of the British people This is evident from the fact that as early as July 1916 a Committee was appointed under the chairmanship of Lord Balfour to study the commercial policy which Great Britain should follow at the end of the War, with special reference to the following questions [1] (a) What industries are essential to the future safety of the nation, and what steps should be taken to maintain or establish them (b) What steps should be taken to recover home and foreign trade lost during the War, and to secure new markets (c) To what extent and by what means the resources of the Empire should and can be developed (d) To what extent and by what means the sources of supply within the Empire can be prevented from falling under foreign control.

The recommendations[1] of the Committee are very instructive, as they emphasised the need of reversion to protectionism Firstly, the Committee stressed the need of fresh legislation to prevent dumping on the lines adopted in Canada Secondly, the British 'Key' and pivotal industries should in their opinion be maintained at all hazards and at all expense Thirdly, they advocated protection by means of customs duties, or government assistance in other forms, of carefully selected industries, which must be maintained either due to the reasons of the national safety or on the general grounds They held that it is undesirable that any industry of real importance to the economic strength and well-being of the British people should be allowed to be weakened by foreign competition or brought to any serious extent in this way, or the other ways, under an alien domination or control Fourthly, preferential treatment should be accorded to the British Overseas Dominions and Possessions in respect of any customs duties now or hereafter to be imposed in the U K, and consideration should be given to other forms of imperial preference Fifthly, the duties imposed should be utilised for commercial negotiation with the allies and neutrals Sixthly, a strong and competent Board should be established, with an independent status, to consider the different forms of State assistance

After the close of the Great War the protectionist policy was strengthened by enacting in October 1920 the Dyestuffs Import Regulation Act, prohibiting the importation, except under licence, of all organic dye stuffs colours and colouring matters An Advisory Committee was set up consisting of five representatives of the colour using industries, three representatives of the dye-manufacturing industries, and three independent members including the chairman, to control the imports and assist the Board of Trade in granting licenses The Act also provided for a Committee to advise the Board of trade in improving the efficiency of the British dye making industry

1 Supra, B T J May 1918 p 563

In August 1921, the Safeguarding of Industries Act was passed, consisting of two parts, the first part provided protective duties to a number of key industries, and the second part empowered the Government to prevent dumping According to the first part, customs duty of one-third of the value was to be imposed on certain scheduled goods imported into Great Britain Such duties, however, were not chargeable on goods consigned from and grown, produced, or manufactured in the British Empire Thus, once again imperial preference became an important feature of the British commercial policy All these provisions were to remain in force for a period of five years so that at the end of that period the Government may be able to examine the situation The schedule included about 6 000 articles chargeable to duty The Board of Trade was empowered to issue lists from time to time defining the articles which were to be taken as falling under any of the general description in the schedule Addition to and exclusion from such a list depended upon the judgment of a referee, appointed by the Treasury, whose decision was final It is significant to note that at that time about one-third of the commodities included in the schedule were not produced in the U K which shows that the new legislation was directed not only to protect existing industries, but also to encourage the establishment of new ones The chemical industry belonged to this category Before the war England depended upon Germany for the products of the chemical industry and as an object lesson she decided to develop a national chemical industry

For the prevention of dumping elaborate provisions were made It was laid down that if on a complaint it appeared to the Board of Trade that imported manufactured goods, other than articles of food and drink, were being sold in the U K at prices below the cost of production in the country of origin, or at prices which by reason of currency depreciation were below the prices at which similar goods could be profitably manufactured in the U K, the Board might refer the matter for enquiry to a

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Committee constituted for the purpose If the Committee recommended that the above conditions were fulfilled the Board might order that the goods be charged a customs duty of one third of the value in addition to any other duty chargeable The Committee of Enquiry was to consist of three persons selected by the President of the Board of Trade from a permanent panel approved by him, consisting of persons of industrial and commercial experience [1] Thus, the Act provided protection not only against industrial dumping but also against dumping resulting from currency depreciation The provisions for depreciated exchanges were to remain in force for a period of three years, and to expire automatically at the end of that period This was expected to protect the British industries against the post-war currency depreciation of the European countries

Thus the Safeguarding of Industries Act introduced excessive protection in England much above that recommended by the Balfour Committee According to that Committee a duty of 10 per cent upon certain commodities connected with the essential industries was sufficient to meet the needs of the conditions created by the War Even this duty would have created a sufficient stir in other countries and led them to strengthen their own tariff walls But as it was, the Act of 1921 raised the level of maximum duties to the extraordinary level of 66-1/3 per cent or 33-1/3 per cent in addition to any existing duties Similarly the anti-dumping measures were not justified by the prevailing economic conditions After the heavy strain of the War no European nation could safely resort to industrial dumping on a large scale This was essentially a period of rehabilitation and therefore the countries all over had to be very cautious in their commercial policy Therefore, it has been rightly remarked that England was fighting against an imaginary danger [2] The measures against currency depreciation were equally harmful, though in this case fears were not entirely unwarranted These measures

1 Vide, B T J 9-6-1921 p 625
2 Vide De Bordes, p 112

were directed chiefly against Germany and created an anomalous situation. Germany was made to pay reparations which she could do only by exporting goods and services but these currency measures penalised German imports

In the evolution of British commercial policy Mr Churchill s budget of 1925 plays an important part He imposed admittedly protective duties on a number of articles Silk was subjected to protective duties varying from 1s 5d. to 7s 9d. per lb, subject to a reduction of one-sixth of the duties on imports from the Empire On artificial silk, duties varied from 1s to 3s 6d., subject to a preference of one-sixth on Empire produce Imported hops were subject to a duty of £4 per cwt, with a preferential reduction of one-third on Empire hops Then followed 33.3 per cent ad valorem duties with a preference of one-third for Empire products, on the following articles clocks watches and component parts, motor cars and cycles, including accessories and component parts, and cinematograph films Finally came a group of safeguarding duties of 33.3 per cent on lace and embroidery, imposed for a period of five years with a preference of one-third for Empire products Before the end of the year, the protective duties of 33.3 per cent ad valorem were imposed on cutlery, gloves and gas mantles with a preference of one-third for the goods of the Empire These measures carried the policy of protection much further Besides the duties imposed under the first part of the Safeguarding of Industries Act of 1921 for a period of five years, expiring on August 19, 1926 were extended for a further period of ten years Mr Churchill, as Chancellor of the Exchequer, declared that the industries thus protected were essential factors in national defence

In the meantime, the British tariff policy recorded a slow but subtle change from safeguarding to subsidies and bounties "The original safeguarding of industries policy" as pointed out by Mr Churchill in 1925, "proposes the

safeguarding of industries by duties imposed from time to time against exceptional competition of particular countries There has been a change in that respect, as was fully admitted to the House We, therefore, abandon that principle of safeguarding against particular countries by discriminating duties, although the anti-dumping provisions embodied in the Safeguarding of Industries Act still remained *in full effect Instead we propose to give effect* to the safe-guarding policy by duties of a general character —general duties "[1] The subsidy granted for a period of ten years on a diminishing scale to sugar manufactured in England from home-grown beet, coupled with a minimum price to the growers in the initial stages, shows the change in the policy The effect of this subsidy was, as Mr Hurst rightly remarks, to induce farmers to grow at the public expense an unprofitable crop of beet sugar instead of growing at their own expense a profitable crop of turnips [2] In view of this accepted policy, coal industry was also granted a subsidy in 1925, but it lapsed within a period of nine months

In short, most of the industries thus protected seem to be relatively less important, for none of them can be regarded as basic or 'key' industry Most of these protected industries were started during the war, but could not face competition after the declaration of peace and resumption of the normal commercial relations Therefore, the Government extended protection to these industries lest they should be swept away by foreign competition But notwithstanding the substantial protection accorded to these industries, they have remained in a precarious condition, unable to face foreign competition This is not all Serious doubts are entertained whether they will be able to face an open competition in the near future If so, they will require a fairly protracted dose of protection which has already proved very costly, apart from strengthening the tendency towards economic nationalism

Thus, before the inception of the depression British commercial policy had assumed the form of extreme protectionism and the portents of its further extension in the same direction were sufficiently conspicuous This extreme attitude proved too costly, because other countries also adjusted their tariffs accordingly It marks the dawn of autarky

FRENCH COMMERCIAL POLICY

We shall now briefly review the French commercial policy The modern commercial policy of France goes back to the Revolution of 1789, which enabled her to establish a common and uniform tariff in place of the multiple provincial tariff systems The tariff thus established in 1791 was fairly moderate But the war of 1792 cut short this liberal commercial policy and thereafter France resorted to restrictive measures The then existing commercial treaties were annulled and concerted efforts were made to eliminate the influx of British goods The duties were raised substantially For instance, the duty on sugar which was a franc per kilgo rose to 4 francs per kilgo Yet the manufacturers were dissatisfied and clamoured for higher protection This over-dose of protection stimulated artificial industrial expansion and created vested interests, which subsequently obstructed the adoption of a liberal tariff policy

The Restoration Monarchy in 1814 tried to revert to a more liberal commercial policy since with the restoration of peace the necessity for the war-time emergency measures did not exist Prohibitions had to be given up and excessive tariff duties to be reduced to moderate dimensions But the vested interests put in a very strong and concerted opposition to this change in policy and succeeded in getting an extension of the protective measures with slight changes The Act of 1816 therefore, did not make any important breaches in the protective tariff In fact, during the Restoration period, not only was the Napoleonic policy of protection continued, but it was further gener-

alised so as to include the agrarian interests The Tariff Act of 1826 completed the scheme of protection, so as to make France economically self-sufficient Thus, the commercial policy during the Restoration period was dictated by the private and sectional interests which the government could not resist

During 1830-48, France, under the new Monarchy set up by the Revolution of 1830, attempted to relax the rigidity of extreme protectionism, which had become almost a tradition But, since the industrial and commercial interests had a strong-hold in the legislature, no material changes could be effected in the tariff system For instance, the Government proposed that the absolute prohibition of import of grain should be abandoned, and be replaced by an extension of the sliding scale of duties, that the country should be divided into two great districts, instead of four zones, that the price of bread should be taken as an index instead of the price of corn, and that in cases of scarcity the surtax on grain imported in foreign vessels should be suspended Due, however, to a strong opposition, first suggestion alone was adopted, and even that could not be enforced Some reductions in duties were made in 1836 but they did not make any radical departure from the traditional protectionist policy

Under Napoleon III, however, important breaches were made in the French protectionist policy Between 1853 and 1855, the rates on coal, pig-iron, steel, wool, cotton, cattle, meat, wines, etc, were reduced Thus, restrictions on both foodstuffs and raw materials were relaxed Ship-building materials were placed on the free list and the restrictions on foreign shipping were also reduced Above all, the most important measure taken in furtherance of a liberal commercial policy was the commercial treaty negotiated with Great Britain in 1860

The Cobden Treaty, 1860—The Codben Treaty, which was expected to last for ten years, subject to one year's notice on either side, outlines the principles of com-

mercial policy that had to be followed by the parties Each country guaranteed most-favoured-nation treatment to the other, which could also be extended to third parties Britain agreed to abolish certain duties and reduce others —a condition which was immediately fulfilled by Gladstone in his budget of 1860 The French Government, in return, agreed to discontinue all prohibitions and to levy in their stead duties not exceeding 30 per cent ad valorem until 1864 and thereafter 24 per cent During 1860-66 France concluded m.f.n. treaties with Belgium, the Zollverein (Germany), Italy, Switzerland, Sweden, Norway, Holland, Spain, Austria, and Portugal. All these countries agreed to make substantial reductions in duties on French products, and France, in turn, agreed to extend the British-treaty-tariff on the goods imported from these countries This was followed by rapid expansion of the French commerce and industries Imports rose from 2442 million francs in 1861 to 2,867 million francs in 1869, and exports from 1,927 million to 2,822 million francs during the same period.

The phenomenal progress of the French commerce and industries which followed the Cobden Treaty did not satisfy the critics of the new liberal commercial policy. By 1875 the movement for protectionist revival made a nation-wide appeal and hastened the end of free trade policy in France Further, the depression of 1875-80 strengthened the hands of the protectionists As a result of all this an Act was passed in 1881, which radically changed the commercial policy of France

The Act of 1881 substituted specific for ad valorem duties and raised the level of duties on the imports of manufactured goods by an average of about 24 per cent., *in order to strengthen the tariff bargaining power of* France in negotiating commercial treaties. On coffee, sugar, and cocoa, purely revenue duties were imposed. Raw materials and foodstuffs were free or subject to nominal duties *Ad valorem* duties were abolished and

the free list was added to Three principles were laid down for the guidance of those entrusted with the task of negotiating commercial treaties (1) the concessions to be made should not exceed as a whole 24% on the general tariff; (2) specific duties alone should be imposed, (3) cereals and cattle should not be included, so that the Government may have a free hand in cases of emergency The treaties negotiated in the past were either denounced or allowed to lapse, and fresh treaties were negotiated based on reciprocal concessions As a result of the treaties, the new conventional tariff included about 1,200 articles on which the rates of duty were either reduced or conventionalised Thus, in practice, duties were substantially reduced on goods imported from the countries having reciprocity treaties

It is interesting to note that agriculture was left out entirely from the scheme of protection, although it held a very important place in the French economy Nearly one-half of the total population was dependent on agriculture, and the fall in agricultural prices had caused considerable hardship to the farmers Pests and diseases affecting certain crops had further added to their economic difficulties Therefore, the agricultural interests forgot their mutual differences and combined together in order to secure protection for agriculture The election of 1885 settled the issue in favour of agricultural interests, and therefore, import duties were immediately raised on wheat, barley, oats, cattle, meats, and other agricultural products In 1885, the duty on wheat was raised from 60 centimes per 100 kilo to 3 francs, and to 5 francs in 1887 Similarly, the rates were further raised on other articles in 1887 The duty on alcoholic liquors was raised in 1887 to 70 francs per hectrolitre of pure alcohol In 1890, excise duty was levied on certain wines manufactured *from raisins to encourage the wine growers at home* Thus, by 1890 French agriculture secured an all-round moderate protection

The Tariff Law of 1882 further strengthened the tariff wall. The new tariff incorporated the plan of "maximum" and "minimum" tariff, the former to be imposed on all countries which would discriminate in any way against French products and the latter to be used for negotiating commercial treaties Under the new tariff fresh commercial treaties were concluded with most of the European countries To the treaty countries France offered the advantage of her minimum rates and secured their lowest rates in return.

To start with it was asserted that the intent of including minimum rates of duties in the tariff was not protection, but simply the placing of French producers in a position to compete with the foreign producers on even terms In the course of the debates, however, the rates were pushed up and the minimum as well as maximum rates became distinctly protective It cannot be denied that the new Act raised the incidence of protection. The agricultural protection became more broad-based and complete Further, protection to manufactures was entirely renovated and substantially raised. It has been rightly said that the new schedules were much more comprehensive and detailed than those of any other continental tariff of the time The protection they afforded was more adequate than any French industries had hitherto got, and agricultural protection was much above that accorded in any European country then As a whole the tariff was one of the stiffest in the world. This tariff remained in force unaltered for eighteen years

Another important feature of the commercial policy of this period is the principle of colonial preference Imports from the Empire were accorded substantially lower tariff, in some cases the products were admitted free, while in others they were given the benefit of minimum tariff or still lower rates. Similarly, French goods were admitted free into the Empire countries.

Due to rapid industrialisation of the country, the tariff system established in 1892 soon proved inadequate The Act had secured to the agricultural interests all that they wanted, but the manufacturers were dissatisfied with the existing system Moreover, the changes introduced in the tariffs of the European countries in 1903 and the years that followed affected materially the French commercial relations These countries had introduced a greater specialisation in their tariffs Further, the framers of the Act of 1892 had assumed that the "maximum" tariff would be the rule and the "minimum" tariff would be the exception In practice, however, the situation worked out to be just the contrary, the minimum rates had been extended to all the European countries except Portugal, and to numerous non-European countries as well Hence in practice the protection extended to the French industries was much less than anticipated by the framers of the Act Again, the difference between the "maximum" and "minimum" tariffs was on an average only 15 per cent, and as such was ineffective as a weapon in tariff bargaining It was, therefore, felt that duties in the minimum tariff should be raised to give a more adequate protection to the French industry, and the difference between the maximum and minimum rates be increased so as to strengthen the bargaining power of the negotiators of French commercial treaties In view of the aforesaid circumstances the need for tariff revision was pressed by commercial bodies and received full support of public opinion

It should, however, be remembered that in the foregoing demand for a tariff-revision there was no suggestion of any change in the principles guiding the commercial policy of France These principles may be briefly noted First, France preferred the system of "maximum and minimum" tariffs, which permitted her tariff autonomy, so that she could raise her tariffs whenever necessary The same practice was followed by America Germany, on the contrary, adopted a "general" and "conventional" tariff under which she was bound by the terms of the commercial trea-

ties not to alter the conventional tariff during the period specified therein Similarly, no change was desired in the policy of colonial preference The revision, therefore, was purely in respect of rates of duties

The Tariff Act of 1910.—The new Act increased both the maximum and minimum rates of duty affecting about 500 out of 654 tariff numbers, and widened the difference between the two schedules of duties In fact, the difference between the maximum and minimum rates of duties was raised above 50 per cent in all cases covered by the revision Agricultural products were left untouched and free admission of raw materials was continued Further, the revision incorporated new headings and a highly developed specialisation This however, did not affect the commercial relations of France with foreign countries, the new law simply substituted a new set of duties for the old one Thus in 1914, when the War broke out, all countries trading with France, except Portugal, were enjoying minimum rates of the French tariff, maximum rates being practically inoperative In short, the new Act introduced only partial changes in the tariff rates laid down by the Act of 1892, its character and essential features remained intact

etc., by prohibiting the importation of less important goods Another important reason advanced for maintaining the policy of prohibition was the necessity of giving more vigorous protection to the domestic industry during the period of economic reconstruction It was felt that prohibition would accomplish this purpose better than an increase of customs duties Besides, prohibition would prevent increase in the national debt and exchange depreciation

But, the policy of prohibition was vigorously opposed on the ground that it raised the cost of living Therefore, the Government abolished prohibition on a large number of commodities and imposed ad valorem surtaxes in addition to the duties in force The rates of surtaxes varied from 10 to 40 per cent for the "maximum' tariff, and 5 to 20 per cent for the "minimum" tariff They were intended to make good the deficiency in the protective effect of the tariff resulting from general rise in prices The surtaxes were imposed on the goods contained in all tariff items, including practically all the manuactured goods

It has already been pointed out that the French tariff of 1892 as an instrument of bargaining, was rather rigid and did not allow the Government to vary its concessions so as to make them equivalent to the advantages obtained from the foreign country, in negotiating a commercial treaty Even the Tariff Act of 1910 did not make any radical changes in the system except some variation in the rates Therefore it was felt that the bargaining power of the Government in negotiating commercial treaties should be increased Accordingly an Act was passed in July 1919, empowering the French Government to negotiate within the limits of the rates of duties contained in the "maximum" and "minimum" schedules an intermediate rate in return for definite concessions granted by the other party to the agreement In case of an article subject to a duty of 100 francs in the "maximum' tariff and of 50 francs in the "minimum" tariff, and in respect of which

the Government under the present law conceded, in a commercial agreement, a reduction of, say, 50 per cent. of the difference between the two tariffs, the rate of duty applicable would be 75 francs[1] Thus, the new system enabled the French Government to negotiate commercial treaties on a basis of strict reciprocity But the greatest defect of the new system was the exclusion of the Most-Favoured-Nation-Clause from the commercial treaties, which added to the difficulties of the French Government in negotiating the same

The Act of 1920 abolished the system of surtaxes and substituted instead the system of "co-efficient of increase," which intended to secure for the French industry and commerce same degree of tariff protection which operated at the outbreak of the War This new system consisted in multiplying the specific rates contained in the pre-war tariff by a co-efficient or multiplier, varying from 1 1 to 3, which was calculated in each case to represent the relation between the official valuation of goods in 1918 and the corresponding value of 1913 The co-efficient 3, which was the maximum fixed, represented an increase of 200 per cent of the pre-war duties This measure was defended on the ground that specific duties imposed by the Act of 1910 could not offer an adequate protection in a period of rising prices This was so, because the effect of specific protective duties varies inversely with the rise in prices, whereas the degree of protection afforded by *ad valorem* duties remains undisturbed under such circumstances

As the French tariff did not prove effective in protecting the French industry and commerce, a Presidential Decree was issued in 1921, providing for an increase of maximum rates of import duty under most of the tariff headings, varying from about 50 per cent to 200 per cent. As a result of this increase, the difference between the rates of duty applicable under the "maximum" and

1 Vide, B T J., 14-8-1919 p 202

"minimum" tariff increased from 100 per cent to about 300 per cent in varying proportions This measure extended a more adequate protection to the French industries against the competition of foreign countries with depreciated currencies

All the maesures discussed above were taken under the Law of May, 1916, which empowered the Government to modify customs duties by administrative action This law, however, not being further extended, expired in December 1922 Henceforth customs duties could be modified only by a special legislation The Government tried several times to re-acquire the power to modify customs duties by decrees, on the ground that in view of the depreciation of currency prompt modifications in duties were desirable But the Parliament always refused to grant such powers The result was that the French customs tariff, as it stood at the end of 1922, became relatively stabilised

In 1926, however an extremely difficult position of national finances necessitated a revival of tariff legislation An Act was passed in April 1926, providing for an increase of 30 per cent in the specific duties applicable to all the dutiable articles except paper and paper-pulp In May of the same year an expert committee was appointed to inquire into and report upon the country's financial situation which was growing worse The Committee held that "the French customs duties represent at present less than half in amount those existing in 1913, if account be taken of the rise in prices and the depreciation in franc"[1] A radical tariff revision was therefore, necessary to secure an adequate protection to industry and a steady yield of revenue For this purpose a new tariff should be adopted without delay, capable of an automatic modification in keeping with the general index number of internal prices

The Act of August 1926 conferred upon the Government the power to adjust by decrees specific duties, taxes, and

1 Vide B T J, 15 7 1926 p 70

imposts to the value of the currency, provided the rates were not increased more than six times those in force in July 1914, or, in the case of duties created after that date, to more than six times the original rates The decrees under this Act had to be submitted to the legislature for ratification Under this authority, a decree was issued in August providing for a further increase of 30 per cent in specific duties

The foregoing study brings to relief the inelasticity of the French customs tariff during the post-war period, and its extremely complicated structure resulting from frequent changes in the co efficient and general rates of duties Ever since the introduction of co-efficients of increase in 1919, the customs duties have been constantly changing in an attempt to adjust the tariff schedules to the ever-changing level of prices Still, protection afforded by these measures did not meet the requirements of the French industries The reconstruction of industries in the devastated regions and restoration of Alsace-Lorraine to France, together with the newly created or recently developed industries, created an entirely new situation, with the result that the existing custom legislation proved entirely inadequate These new industries included the chemical and metallurgical the mechanical trades in general, and the automobile factories in particular Another important reason for an early revision of the existing tariff was the necessity of a more stable tariff with which to enter into commercial treaties with foreign countries and provide thereby a more stable basis for international trade In short, the French customs tariff needed greater stability than it had been able to achieve since the close of the war.

In March 1927, a Bill was introduced for the revision of the French customs tariff The new measure retains the classical form of the two schedules, the "maximum" and the "minimum," with the possibility of reducing the rates of duty below the minimum tariff in the negotiation of

commercial agreements with foreign countries The Bill outlines only the minimum rates of duty, and the maximum tariff will be in almost all cases three times as high as the minimum The system of specific duties, which was abandoned in 1919, has been reintroduced In support of the new system it was said that the application of ad valorem duties in France is very difficult and complicated owing to the organisation of the country's customs administration, and that such duties substantially increase the cost of living in times when prices show a general upward trend Hence, the number of *ad valorem* duties was reduced to an indispensable minimum

The system of co-efficients of increase, characteristic feature of the post war tariff policy of France, has been replaced by a new element of variability for adjusting the duties with changes in prices The Government is authorised to revise the tariff every three months, whenever variation in the general index of wholesale prices is 20 per cent or more

The Bill also effected a general increase in the rates of duties The manufactured products, including luxury food-stuffs, were taxed most heavily Raw materials were either exempted from duties entirely or charged low rates But a number of maximum rates applicable on certain raw materials have been introduced as retaliatory measures to secure equitable treatment from countries enforcing unduly high tariffs on the French goods The duties on agricultural products were also increased in order to achieve self-sufficiency In short the new French customs tariff secured greater protection to both manufacturing industries and agriculture This policy adopted to reserve the domestic market for the French industries was continued till the inception of the depression

Before we close our review of the pre-depression French commercial policy it is essential to note the commercial treaties negotiated by France during the post-war period In November 1920, an accord was negotiated with Czecho-

With Canada an agreement was entered into in December 1922, under which, in exchange for m f n treatment accorded by Canada to the French goods, France granted the benefit of the "minimum" tariff on 125 Canadian goods and accorded reductions varying from 15 to 85 per cent. of the difference between the "minimum" and "maximum" tariffs on about 400 articles[1]

A commercial treaty was concluded with Austria in July 1923 France gave the benefit of her "minimum" tariff on a number of Austrian goods, but in some of these cases the benefit was limited to a fixed annual amount On some of the other articles, France granted reductions varying from 30 to 80 per cent of the difference between the "maximum" and "minimum" tariffs

France negotiated an important commercial treaty with Germany, in August 1927 Under the treaty, France, in return for valuable concessions on the French goods imported into Germany, granted the benefit of minimum rates on a large number of German products Besides, reductions averaging 50 per cent of the difference between the "maximum" and "minimum" tariff were granted on various other German products

Thus, as a result of the post-war commercial treaties negotiated by France, the customs barriers were substantially reduced The reductions averaging 40 per cent of the difference between the "maximum" and "minimum" rates, and the granting of the benefit of the "minimum" rates conceded through these treaties, affected more than one-third of the total foreign trade of France, with the result that the protective character of the high duties of the general tariff was considerably reduced[2] Further, the principle of "intermediate" tariff was incorporated in the post-war French tariff structure Thirdly, the M F N Clause was made applicable only to the "intermediate" rates

1 Vide B T J 22-3-1923 p 362

2 Vide Delle Donne p 187

GERMAN COMMERCIAL POLICY

The industrial system of modern Germany is a marvel of human genius Its evolution should, therefore, be carefully studied Protection is a tradition with the Germans, and free trade an infraction of that tradition The evolution of German commercial policy amply supports this statement In the beginning of the nineteenth century, German States extended tariff protection both to agriculture and industries Besides Germany was split up into a number of independent States with their own individual customs areas and tariff walls There were in operation in Prussia in 1800 more than sixty different tariffs covering about two thousand eight hundred classes of goods, and ranging all the way from extreme protectionism in the form of complete prohibition of the import for foreign manufactures in some provinces to the free importation or moderate tariffs in others [1] No wonder, therefore, that as a result of this multiplicity of restrictions German trade and industries suffered

The reforms of 1818 improved considerably the chaotic conditions in the German tariff system All internal customs barriers were abolished and the country was fortunately for the first time united into a compact customs union Raw materials were freed from import duties and other restrictions in order to enable the rising German industries to reduce their cost of production Imports of manufactures were, however, subject to an average duty of 10 per cent the rates being lower in the western provinces as compared with those in the east The import prohibitions were entirely abolished, with the sole exception of the Government monopolies Thus, on the whole, Prussia had a more liberal commercial policy than that of any other continental country [2]

Further, Prussia realised that for a well-ordered development of the German industries and commerce it was

essential that the mutual jealousies between the different States and duchies should be checked and a common understanding be arrived at in the interests of the country as a whole Therefore, right from 1818 Prussia pursued a policy of enforced commercial assimilation and compelled the smaller States to accept common tariff arrangements, under which trade between the States was to be free from restrictions But the policy of enforced absorption aroused apprehensions in some of the States about the intention of Prussia and led to the foundations of a separate union This was an object lesson to Prussia to reconsider her attitude of compulsion towards the other States Under the circumstances, the right attitude for Prussia to adopt was that of voluntary co-operation, and that she fortunately did The result of this conciliatory attitude was that a number of States joined the Prussian union and the other competing union soon disappeared Under the new arrangement, the tariff policy was to be determined by a conference of delegates of the affiliated States, giving thereby a hand to all the member-States in moulding the form of commercial policy The changes to be introduced must have a unanimous appproval of the members Further, a common tariff was to be enforced against all the States outside the union, but each State was permitted to retain its individual commercial code and monopolies Trade within the union was to be free from tariff restrictions The customs receipts were to be divided among the member States in proportion to their population Raw materials were placed on the free list, and moderate duties were levied on imports of manufactures Duties for revenue purposes were levied on the colonial produce The terms of the agreement, upon which the union rested, were formally renewed at the intervals of twelve years, in 1841, 1853 and 1865

It is interesting to note that during this interval the teachings of Fredrich List had a marked effect on the protectionist revival in Germany and elsewhere He rightly argued that the economic laws are relative to the

stage of economic development that a country has attained, and hence the commercial policy which a country adopts must suit its economic requirements England, with the aid of protective tariff, had attained a stage of industrial development when the continuance of protectionist policy became needless and wasteful for her In Germany, however, the economic conditions were materially different, the transition had yet to be effected, and till then protection for the German industries was indispensable He pleaded for a reasoned policy of protection for Germany This argument had a wide apppeal and strengthened the hands of the protectionist element in the country Therefore, we find a steady increase in duties during 1843, 1844 and 1846

But the protectionist movement soon received a setback and could not be revived for a long period. For about a quarter of a century we had an era of relatively low tariffs in Germany due, inter alia, to the growing ascendancy of Prussia in the German politics Prussia's commercial policy was dictated by the agricultural and commercial interests, she exported large quantities of agricultural produce and imported agricultural machinery Further, the German Economic Congress, established in 1858, moulded the public opinion in favour of free trade In 1862 Prussia negotiated a commercial treaty with France on the lines of the Cobden Treaty, which helped to further the cause of free trade The defeat of Austria by Prussia in 1866, and the establishment of the North German Confederation thereafter, enabled the latter to reduce tariffs In place of the old customs union was erected a new customs union in 1867, and it was agreed that the changes in the customs tariff may be made by a vote of the majority instead of the assent of every member-State This enabled Prussia to carry through the policy of free trade with sufficient force In 1868 and 1870 the tariff was simplified and duties lowered. Thus, before the establishment of the Empire, tariffs were fairly low

According to the Imperial constitution, Germany formed one customs and commercial territory with a common frontier for collection of duties Further, the Empire had exclusive power to legislate on customs matters The collection of both customs duties and excise was left to the States, subject to the supervision of the Imperial officers After deducting the cost of collection and protection of the frontier, the receipts belonged to the Imperial treasury and had to be returned forthwith After 1879, however, the States were permitted to share the proceeds During this period, the policy of free trade was rapidly pushed through In 1873 the import duties on agricultural machinery were lowered By 1875 the Imperial tariff had been shorn of its protectionist features, so that what remained was a purely revenue tariff, about 95 per cent of the imports were duty-free Thus the German Empire became very nearly a free-trading State

All these measures were carried through in the teeth of strong opposition, particularly of the industrialists This free trade policy however, did not last long The protectionist proclivities of the German people were gradually strengthened and a new orientation given to the German protective tariff The German agriculturists who had hitherto supported the case for free trade in order to find an open world market for their produce found that their own market was flooded with cheap American and Russian imports No wonder therefore that the German agriculturists gave up their grandiose hopes of capturing world markets under free trade, and thought it expedient to take prompt measures for protecting their own home-market by protective tariffs German industries also suffered severely during this period from the competition of well-established British industries and therefore joined the agricultural interests in their claim for tariff protection This protectionist revival received full support from the State with Bismarck at its head A new tariff Act was passed in 1879 which marked the advent of a new protectionist era for Germany, which continued

uninterrupted up to 1914 The Act was, however, fairly moderate and introduced a purely revenue tariff Some of the important raw materials were on the free list But the tariff system was inelastic, and unscientific, in particular it did not take sufficient account of the complications of the structure of industry, and lacked adaptability [1] To this must be added the additional agricultural protection extended in 1881, 1885 and 1887

The neighbouring countries did not approve of Bismarckian policy, which had been in force for about a decade, and proposed to terminate the reciprocal m f n agreements Besides, Bismarck himself lost his political prestige and power and was succeeded by Caprivi, who adopted a more conciliatory commercial policy He abandoned the principle of tariff autonomy and entered into a series of trade-agreements based upon the principle of reciprocal reduction of duties Between 1891 and 1894, trade agreements were negotiated with Austria-Hungary, Italy, Belgium, Switzerland, Rumania, Serbia, and Russia All these commercial treaties provided for the m f n treatment and mutual reductions and remissions of duties The agreements were to continue until the end of 1903, and hereafter indefinitely until terminated by either party by giving notice of one year This new attitude was in accordance with economic conditions of the country, which had in the meantime changed considerably German industries, under the influence of protectionist policy, had reached such a stage of development and progress that the home-market was no longer sufficient to absorb the constantly increasing production, and new outlets abroad were badly needed This purpose could be conveniently achieved by commercial treaties [2]

Thus, Germany once again adopted the system of autonomous and conventional tariffs, the former to be applied to those countries which did not enter into a trade-agreement providing for reciprocal trade concessions, and

the latter contained reduced rates, applicable on goods imported from countries having commercial treaties with Germany The German tariff system, however, was radically different from that adopted by France, because whereas in the case of France both the maximum and minimum duties could be raised at any time, the German Government bound itself under the treaties not to increase the rates for a term of years

The agrarian interests, however, continued their agitation against the new policy and soon acquired considerable influence in German politics In 1901 they succeeded in getting a pledge from the then Chancellor for a substantial increase of duties on grain, live-stock and all other agricultural products Accordingly, the Tariff Act of 1902 was passed The striking features of the new measure were as follows (i) The new Act was much more detailed in character as it contained 946 articles, while the Tariff Act of 1879 contained only 394 articles, of these 200 were to be free of duty, (ii) the duties on most raw materials were reduced, (iii) the duties on grain, live-stock, and meats were greatly increased, while the taxes on various articles of use to the agriculturists were abolished, (iv) with respect to wheat, rye, oats, barley, etc, minimum duties were specified below which reductions by trade-agreements could not be made, and, (v) the duties on manufactured goods were increased

The tariff thus enacted was the general tariff to be applied to the countries which did not enter into commercial treaties with Germany providing for reciprocal reductions of duties and those which did not enjoy the m f n treatment The conventional tariff was to be built up as a result of a series of trade agreements to be negotiated with different countries Pending the negotiation of commercial treaties, the general tariff was held in suspense This specialised higher general tariff represented a powerful weapon in the hands of Germany in tariff bargaining The new tariff aroused suspicion in the

neighbouring countries, with the result that Switzerland, Austria-Hungary, Russia and Rumania immediately raised their tariffs on manufactures, particularly those coming from Germany, in order to strengthen their bargaining power This increased the difficulties of German negotiators Between 1904 and 1905, the new series of commercial treaties were concluded which were to remain in force till the end of 1917, and thereafter indefinitely, subject to one year's notice These treaties effected substantial reductions in the general tariff and guaranteed m f n treatment But, Germany was compelled to accept substantial increases of duties on some articles of importance to her export trade [1] From those countries which did not enter into special commercial agreements, Germany tried to secure the m f n treatment To this category belonged *Great Britain, France*, Spain, Holland, *etc* The *United* States was also accorded the benefit of the German minimum tariff Thus, the general tariff of 1902 seems to have been used primarily as an instrument of tariff bargaining The conventional tariff, based on the new treaties, was most effective in practice, and a better part of German trade was carried under the lower rates But the rates in the conventional tariff were highly protective, particularly those on the agricultural produce and half finished goods In certain cases, however, rates were "conventionalised"

The commercial expansion of Germany from 1870 till the outbreak of the World War remains one of the most interesting lessons of modern economic history No one could have foreseen in 1870 that the poor Germany of that time would become one of the leading economic powers of the world in about fifty years The industrialisation of the country, started with considerable rapidity in the seventies, was definitely accomplished by the end of the nineteenth century Having acquired complete control over the home market, German industrialists started capturing foreign markets The German penetration into

1 Vide, Ashley pp 113-14.

markets hitherto completely and securely controlled by Great Britain represents a masterpiece of ability and pertinacity No wonder, therefore, that Germany became the leader of Continental European trade before the World War, her trade was second only to that of England Exports consisted chiefly of manufactures, and imports mostly of raw materials and food stuffs, affording the best index of advanced industrialisation of the country

The splendid organisation of the German foreign trade and adaptability of German exports to meet the needs and the tastes of the consumers in all markets were the principal factors in stimulating this phenomenal expansion of German trade The German manufacturers and merchants took considerable care in ascertaining the kinds of goods desired by their customers and adjusted the quality, price and terms of payment to suit them

The German banks played an important part in the promotion of foreign trade To a large extent the superiority of German commerce depended upon cheap and adequate credit facilities provided by the German banks To this was added a very efficient information-service, which provided detailed and most reliable information to the German merchants about foreign markets Further, the diplomatic and consular bodies also rendered valuable assistance in developing German trade A well-co-ordinated transport system proved invaluable in penetrating foreign markets The customs tariff strengthened Germany's bargaining power in negotiating commercial treaties and extracting valuable concessions for her industry and commerce Again, the vast and economically developed Colonial Empire in itself provided a fairly wide market for the German goods

Post-War Tariff Policy—The provisions of the Treaty of Versailles deprived Germany of her tariff autonomy *Article 269 of the Treaty provided that for the first six* months from the coming into force of the Treaty, the duties imposed by Germany on imports from all the Allied

and Associated States were not to be higber than the most favourable duties which were applied to imports into Germany in July 1914 During a further period of thirty months this provision was to be applied exclusively to the products which before the War enjoyed rates conventionalised through treaties with the Allied and Associated States But, whereas Germany was obliged to accord to the Allies her lowest tariffs, they reserved for themselves the right to apply to the German imports their most discriminatory tariffs, which they frequently used Thus, Germany was completely deprived of freedom of action in shaping her tariff policy This state of affairs lasted till 1925

Once the restrictions on Germany in moulding her commercial policy were withdrawn, the German Government passed the Tariff Act of 1925 which effected a partial revision of the general customs tariff The revision which affected 400, of the 946, headings of the tariff, not only increased the duties on various classes of manufactured goods, but also levied new or substantially higher duties on agricultural products Thereafter, Germany started negotiating commercial treaties based on the reciprocal guarantees of m.f.n treatment and secured substantial concessions

A commercial treaty was entered into with Italy in October 1925, under which, besides reciprocal guarantees of m.f n treatment, Germany granted reductions on several articles averaging 40 per cent[1] In July 1926, a commercial agreement was entered into with Switzerland It was based on reciprocal guarantees of m f.n treatment, and in addition Germany reduced her duties on an average of 20 per cent on several articles[2] A similar agreement was concluded with Sweden in the same year[3]

In August 1926, a provisional agreement was reached between France and Germany whereby, in return for considerable reductions of French duties on imported

1 Vide B.T J., 17-6-1925, p 701
2 Vide, B.T J., 11 11 1926, p 509
3. Vide, B T J., 12-8-1926, p 180.

German goods Germany accorded reductions averaging 45 per cent on various articles[1] This provisional accord was replaced by a commercial treaty concluded in August 1927 In return for substantial concessions on German goods imported into France Germany accorded the benefit of her conventional tariff In addition she granted reductions averaging 40 per cent on a long list of French products[2]

Thus before the depression set in Germany having regained her tariff autonomy had reorganised her tariff system and negotiated a number of commercial treaties on the basis of reciprocity so as to facilitate the growth of German industries and commerce

AMERICAN TARIFF POLICY

Modern American tariff policy dates from 1782 when attempts were made to resist the aggressive commercial policy of Great Britain and the European powers Here it is interesting to trace definite protectionist elements in the tariff policy It would therefore be no exaggeration to say that in the evolution of American industries and commerce protection has played an important part

The Tariff Act of 1789 imposed specific as well as ad valorem duties which were to remain in force for seven years Specific duties were imposed on thirty six articles of which the more important ones were tea sugar salt molasses spirits steel nails and cardage An ad valorem duty of 5 per cent was imposed on all imports except seventeen raw materials like wool cotton hides dye stuffs etc which were placed on the free list Carriages were taxed at 15 per cent ad valorem and on several other articles duties at 10 per cent ad valorem were levied Paper gloves leather buttons clothing etc were charged 7½ per cent These moderate duties were imposed to meet the growing financial requirements of the Union As they did not suffice to meet the requirements these duties were

1 Vide, B T J 19-8-1926, p 20
2 Vid B T J 1 9-1927 p 27

raised in the very next year. It would, however, be idle to deny that these duties afforded adequate protection to American industries This is not all. The Congress itself was imbued with the idea of rapid industrialisation of the country so as to make her independent of other countries for essential supplies The protectionist features of the first modern tariff Act, therefore, do not come to us as a surprise

Between 1792 and 1816, the tariff legislation was very brisk, due to financial difficulties The protectionist forces, although gathering their strength outside the Congress, could not influence the course of tariff legislation Therefore, during this period America had an essentially revenue tariff, with very few exceptions But the Anglo-French wars afforded invaluable protection to American industries It was during these years that the factory system began to replace the domestic process of production in the United States

The Treaty of Peace and the commercial agreement of 1815 were followed by a rapid influx of British goods in the American market, which threatened the very existence of the infant industries in America, that had grown up under the protection provided by long wars The tariff was, therefore, revised in 1816 Cotton manufactures were taxed at 25 per cent ad valorem for three years and 20 per cent thereafter A duty of 45 cents per cwt was imposed on iron bars But, the contention that this Act was dictated chiefly by a financial stringency, and that the framers had no protectionist bias, is not sufficiently convincing

In 1824 the President invited the attention of the new Congress to the American tariff for the purpose of affording such additional protection to those articles which the United States was prepared to manufacture, or which were essential for the defence and independence of the country The result was the Tariff Act of 1824, which

raised the duties on cotton and woollen goods from 25 to 33 1/3 per cent The duties on iron, wool, hemp, etc, were also increased

The principle of protection was further extended by the Tariff Act of 1828, by which substantial increases were made in the customs duties The duty on hemp was raised from 35 dollars to 45 dollars a ton, on molasses from 5 to 7½ cents a gallon, on pig iron from 56 to 62½ cents per cwt, on rolled bar-iron from 30 dollars to 37 dollars a ton, and on hammered bar-iron from 90 to 112 cents per cwt Rates on woollen manufactures were also raised Thus, the most striking feature of the Act was an attempt to protect the existing American industries and aid the growth of new ones under the tariff wall

The height of the protective tariff spurred the free traders to close their ranks and make concerted efforts to secure prompt modifications in the rates In 1830, therefore, the duty on tea was reduced by 50 per cent The duty on molasses was reduced to the old level and the system of drawbacks permitted

Further tariff modifications were made by the Act of 1832 The cheaper varieties of wool were admitted free, and on others duties were substantially reduced On cheap woollen goods the duty was reduced to 5 per cent ad valorem, and on worsted goods from 25 per cent to 10 per cent The duty on raw flax was abolished and on manufactured hemp reduced by one-third The rates of duty on silk, pig iron, bar iron, etc, were also reduced The number of free articles was increased from 49 to 189 In short, the protective system was moulded so as to suit better the needs of the people

The Act of 1833 recorded further reductions in the protective duties According to this Act all duties in excess of 20 per cent ad valorem were to be reduced by one-tenth of the excess in each alternate year up to 1839, and after that by a greater amount, so that the whole

excess may be abolished by 1841 Some duties were immediately abolished. Thus, by 1842 duties were expected to be brought down to uniform level of 20 per cent, and the free list considerably increased

The Tariff Act of 1842 marks a distinct return to protectionism. The average level of duties was raised to 30 per cent and those on the manufactures still higher The increased protection thus afforded by the new tariff stimulated the growth of American industries and commerce

The triumph of democrats, who were opposed to protectionist policy, in the Presidential election of 1844, resulted in the Tariff Act of 1846 which brought down the general level of duties The duties ranged from 5 per cent to 40 per cent On certain manufactures like iron, woollens, glass, leather, etc., 30 per cent duty was levied. Cotton goods paid 25 per cent The specific duties were abolished, and the free list increased. This tariff remained in force for eleven years without any alteration.

In 1857 the tariff was revised and duties lowered. There was an all round reduction of 20 to 25 per cent, with the result that the highest protective duty under the new system was about 24 per cent ad valorem. The free list was enlarged, so as to include a larger number of raw materials in it

The financial difficulties of the Union and the ascendency of the Republicans to power brought a marked change in the fiscal policy The new Act of 1861 imposed specific duties on iron and steel goods varying from 6 dollars in the case of pig-iron, to about 15 to 20 dollars a ton on iron rails On steel a fairly high combined specific and ad valorem duty was levied. The general effect of the new legislation was to raise the rates above the level of 1846 Thus, the work of the democrats was completely undone

The Civil War which soon followed called for an extensive revision of the tariffs in order to overcome the

financial difficulties of the Union In 1861 duties were imposed on several articles, like tea, coffee, sugar, hemp, hides, rubber, silk, spices, etc, and on other articles duties were substantially increased This was not all The Customs Act of 1864 raised the average level of duties to 47 per cent. This emergency tariff continued even after the close of the war

It was in 1870 that an attempt was made to reduce revenue duties Accordingly duties on tea, coffee, sugar, cocoa, spices, etc, were lowered, and a number of raw materials and foodstuffs were placed on the free list Thus, the tariff, as a whole, was lowered, but the protective duties were an important source of revenue for the Federal Government

The duties were further lowered in 1872 The duties on cotton, wool, woollens, metals, paper, glass, and leather manufactures were reduced by 10 per cent On tobacco and whisky both customs and excise duties were lowered, and duties on tea and coffee were abolished Reductions were also made in duties on coal and steel These tariff changes, made as a concession to the free trade sentiment, in effect increased the dependence of the Federal revenue on purely protective tariff

The Act of 1875 repealed the horizontal reductions made in 1872 and raised the duties on sugar, molasses, tobacco, and spirits The general level of the tariffs was raised to the pitch prevailing during the Civil War

The next revision of the tariff came in 1883 Under the new Act duties on raw wool and woollen goods were reduced On silks the duty was lowered by about 16 per cent, and on steel rails by about 40 per cent Reductions were also made in the case of cotton marble, nickel, copper, barley, pig-iron, etc On several other articles duties were raised To this category belonged manufactured goods Thus, taken as a whole, the new tariff did not record any radical change

The McKinley Tariff of 1890.—By 1890 there was an all round economic development of the country; and with it the American industries and commerce prospered. At this time the United States' industrial position was somewhere between that of the advanced industrialised countries of Europe and the primarily agricultural countries of the Latin America. American industries could not face an open competition of advanced industrial countries The United States was, therefore, prepared to maintain and increase its high tariffs on the manufactured goods But there was an important change in the basis of protection. Hitherto, protection was supported by the infant industries argument. But now this argument could no longer be seriously maintained. The protectionist, therefore, pleaded that the highly paid American workman needed protection against the competition of ill-paid European labour This could be done by imposing such duties on the European goods, imported into the United States, as would counter-balance the disadvantages of the greater cost of production in America, and at the same time afford a moderate protection.

The most important feature of the McKinley tariff was the extension of protection to agriculture The duty on barley was increased from 10 cents to 30 cents a bushel; on oats from 10 to 15 cents, on wheat from 20 to 25 cents, on potatoes from 20 to 25 cents, whilst eggs and apples, hitherto free, were subjected to duties 5 cents a dozen and 25 cents per cent ad valorem respectively On tobacco suitable for cigars the duty was raised from 75 cents to 2 dollars a pound. Similarly, rates or wool were raised substantially

The manufacturers also received an adequate assistance For instance, the woollen industry had a good slice of protection. As the iron and steel manufactures no longer feared the foreign competitors, the duties on the imports of steel goods were lowered. Protection to the tinplate industry was strengthened and the result was that the

manufacturers obtained a firm footing The duty on raw sugar was abolished and on refined sugar lowered to half a cent per pound But, for home producers of sugar, of the best quality, a bounty of two cents per pound was given for fourteen years

The President was empowered to suspend the free list and impose duties on imports from those countries which levied unequal and unreasonable duties on the American goods Thus, the Act provided a penalty method for obtaining concessions Under this Act agreements for reduction of duties were concluded with Brazil, Dominican Republic, Barbados, Trinidad, Leeward Islands Windward Islands, and British Guiana As a result of these concessions American exports received sufficient encouragement when there was a marked tendency to decline The penalty duties were imposed on trade with Columbia, Venezuela and Haiti, and in consequence imports from these countries into America suffered

The Wilson Tariff Act of 1894 abolished the duties on raw wool and substituted ad valorem duties on woollen goods in place of specific duties On a number of commodities the duties were reduced by about 50 to 75 per cent In some cases like sugar, molasses, meat rye barley etc, the new Act imposed higher duties Further, the Act repealed the provision giving power to the President to impose penalties This brought to an abrupt end the commercial treaties entered into under the Act of 1890, and caused heavy losses to those countries which had invested huge capital in industries relying primarily on free access to the American market This shows the dangers of uncertainty and sudden reversals in commercial policy

The Dingley Act of 1897—To meet the fiscal requirements of the Treasury the Dingley Act was passed in 1897, which raised the level of tariff duties Raw materials, like wool, flax, hides etc, were again subjected to duties On the manufactured goods—woollens, cotton, silk, iron

and steel, etc,—duties were raised On raw sugar a specific duty was imposed, the incidence being doubled

This Act also contained provisions for tariff bargaining similar in character to those embodied in the Act of 1890 There was, however some change in the list of duty-free articles Sugar, molasses, and hides were excluded from the list and instead coffee, tea, tonka and vanilla beans were put in This new list of duty-free articles was comparatively less important and, therefore, the bargaining power was much less effective The most important commercial agreement entered into under the new regime was that with Brazil, whereby the American imports into Brazil received valuable concessions

Commercial treaties were also negotiated with France, Germany, Italy, Portugal, Switzerland, Spain, Bulgaria, and the Netherlands, but they could not yield substantial benefits Minor reductions and remissions in duties were obtained

The Tariff Act of 1909 strengthened the bargaining power of the United States The Act adopted "maximum" and "minimum" tariff to provide for commercial reciprocity The President was empowered to decide whether a country was discriminating against the American goods There was an extensive re-classification of commodities, and numerous alterations in the rates of duty were made All bounty-fed imports were to be subjected to surtaxes equal to the amount of the bounties, as determined by the Treasury after due enquiry When imported materials on which duties had been paid were used for manufacturing articles in the United States, there was to be allowed on the exportation of such articles a drawback equivalent to 99 per cent of the duties paid on the materials used An additional duty of 10 per cent ad valorem, was to be levied on all goods not imported in the United States vessels, except in the case of goods imported in vessels of a country entitled to national treatment in respect of shipping and navigation

After a detailed investigation the "minimum" tariff was extended to all countries except Germany, France and Canada With these countries, also, negotiations were carried on as a result of which discrimination on American goods was removed and benefits of the "minimum" tariff extended to them

The tariff Act of 1913 marked the complete reversal of tariff policy the United States had pursued hitherto The principle of "maximum" and "minimum" tariff, which had strengthened the bargaining power of the United States on the basis of reciprocity, was abandoned Further, the tariff classification was radically recast and minute subdivisions of different classes of goods removed This lack of specialisation weakened the bargaining power of the United States still more To this must be added the abolition and reduction of duties in numerous cases Ad valorem duties were substituted in place of the specific ones in a large number of cases which increased substantially the cost of administrative machinery Finally, the President was empowered to negotiate commercial treaties on the basis of reciprocity, subject to the approval of the Congress Thus, it is clear that by 1913 the structure of American industries had improved sufficiently so that they could face foreign competition, protection had fulfilled its purpose

The World War of 1914-18 created extremely abnormal conditions and secured to the American industries full-fledged protection amounting to prohibition Further the War intensified the feeling for national self-sufficiency The protectionist sentiment therefore gathered new strength throughout the world under the guise of economic nationalism "The trend towards protection strong enough before the War, became even more strong after its close "[1]

With the severe decline in prices in 1921 the agitation for protection gathered strength Therefore in 1921 an

1 Taussig F W "The Tariff History of the United States p 450

Emergency Tariff Act was passed, it imposed high duties upon wheat, corn, meat, wool, sugar, etc But the high tariff duties failed to improve the situation due to continuous decline in prices

The Tariff Act of 1922—The new Act effected a substantial increase in duties on agricultural commodities and extended the list of duties so as to include almost every commodity Agricultural implements continued to be admitted free The protection to textile industries was generally the same as had been hitherto maintained But the policy of protection was carried to extreme limits in the case of metal articles toys, chinaware, cotton gloves, laces, pocket knives, razors, rifles, guns, dyestuffs, etc

Further, the Act empowered the President to impose penalties upon the commerce of any country which should discriminate against the products of the United States If the discriminating country should refuse to end its unequal treatment, the President may place new or additional duties upon the importation of any or all of its products not exceeding 50 per cent ad valorem. If, even then, the discrimination does not cease, the President may proclaim the total prohibition of importation of such goods from that country as he may deem the public interest may require It is however, interesting to note that this clause is essentially different from the penalty clause of the Act of 1890 in that it seeks to secure equality of treatment and not concessions in favour of the United States The American industries could now successfully compete with those of the advanced industrialised countries of Europe

In short, during the post-war period there has been a material change in the United States' commercial policy due to the increased efficiency of American industries Reciprocity, special favours, and the conditional interpretation of the M F.N Clause were abandoned and instead an equal opportunity in the markets of the world was demanded. Thus, before the depression set in, the

structure of the American industries and commerce had improved sufficiently to dispense with protection

Conclusions—We shall now briefly summarise the conclusions that may be drawn from the foregoing study of tariff policy

(i) *Protective tariff has played an important part in stimulating the growth of modern industries and commerce*

(ii) A moderate policy of protection, determined by the reasonable national economic requirements helps the most efficient utilisation of national resources and maximises thereby the national dividend

(iii) An expert, independent, and permanent tariff board must be entrusted with the task of studying the working of tariff policy so as to be able to eliminate wasteful tendencies

(iv) The uncertainty and sudden reversals in tariff policy are dangerous and should be eliminated

CHAPTER II

COMMERCIAL POLICY SINCE THE DEPRESSION

A DETAILED analysis of the pre depression tariff policy has shown the attempts made by more important countries to foster the growth of industries behind tariff walls With the inception of the twentieth century this tendency received an added stimulus due to certain political and economic maladjustments The Great War shattered the hopes of the supporters of free-trade by demonstrating the vulnerability of the economic system based on laissez faire No wonder therefore that the general level of tariffs have been gradually rising during the post war period The economic readjustment necessitated by these changes has been difficult to effect The constant fluctuations in tariff levels have further aggravated the difficulties As a result we find a marked shrinkage in foreign trade and the problem of surplus productive capacity in advanced industrialised countries which are faced with dwindling markets Hence the need for a critical study of the economic policy during and since the depression Before however we proceed to analyse the commercial policy during the depression we may consider briefly the forces which led to it

The improvements in the means of communications and the geographical division of labour have made the entire world a closely knit economic unit so that the national prosperity in the modern world depends upon the smooth working of international economic relations The economic and political upheavals of the twentieth century have transformed the structure of modern industry and created new problems The craze for economic self sufficiency resulting from political and economic insecurity has turned the otherwise homogeneous economic entity into a group of nations at war with each other pursuing divergent and contradictory policies The most obvious result of all this is self frustration.

Political Insecurity.—The growing ambitions of the imperialist powers led them into the Great War and the Treaty of Versailles sanctified and spurred the greed The establishment of the League of Nations, the Locarno Agreement of 1925, and the Kellog Pact of 1928, intended to inaugurate an era of international co-operation and goodwill, failed to inspire sufficient confidence amongst countries groaning under the weight of the treaty obligations If the political atmosphere remained quiet it was because the countries had not gathered sufficient strength to revolt openly against the wanton inroads upon their liberties Mutual suspicion and distrust have been rife amongst different nations This had conspicuous results upon the commercial policy Although the world trade during 1925-29 recorded a considerable increase, it was essentially temporary, the economic stability was lacking The Peace Treaty had increased the number of countries in Euope, each of which set up new trade barriers to protect national industries, and the range was gradually extended to include the whole of the industrial and agricultural activity

Monetary Instability—A monetary standard to be useful, must secure to the people internal as well as external stability of the unlimited legal tender money In the pre-war days gold standard achieved marvellous monetary stability This was so because short-term capital movement helped to equalise the balance of payments due to absence of war scares To this should be added the credit policy of the central banks, which effected prompt and direct adjustment of trade balances Countries with an adverse balance of trade had to export gold to meet their obligations and restrict internal credit facilities This lowered the internal price level reducing thereby the imports and stimulating exports The countries with a favourable balance of trade used the gold received in adjustment of the trade balances for lowering the discount rates and increasing the credit facilities This expensive credit policy stimulated imports and discouraged exports

Thus, the adjustment of exchange was automatic before the Great War

The abnormal conditions during the War led to an unprecedented inflation and upset the currency systems of the belligerent countries After the close of the War, attempts were made to improve these chaotic currency conditions, which had undermined confidence and checked an economic rehabilitation The Monetary Conference held at Brussels in 1920 and at Genoa in 1922 made distinct contributions towards the stabilisation of world currencies There were two alternatives available (1) the return to the independent currency systems with fluctuating exchanges, or (ii) an international currency system with stable exchanges and a correlated price and income structure The second alternative was accepted by the Genoa Conference Soon after, most of the important countries stabilised their currency systems Great Britain returned to the gold standard in 1925 and by 1929 a number of advanced countries had adopted either the gold standard or the gold-exchange standard

The working of the gold standard during the brief span of 1925-29 showed very creditable results, supporting the contentions of those who believed that the restoration of the gold standard would remove the economic, financial, and monetary disequilibrium existing in the war-exhausted economic systems [1] The marked increase in the world trade and commerce during this period bears out the claims

But the different levels at which world currencies were stabilised created complications Great Britain established a gold-parity which meant that her existing level of sterling income and costs were relatively too high in terms of gold, so that, failing a downward adjustment, those of her industries which were subject to foreign competition were put to an artificial disadvantage [2] Under the normal working of the gold standard, as it had functioned during

1 Vide Gregory, T E "Gold Standard and its Future" p 13

2 Committee on Finance and Industry p 106

the pre-war period, the necessary adjustments would have been automatically effected within a very short time But the war had created new problems of commercial policy The rigidity of the post-war price and income structure obstructed the adjustment

Another group of countries stabilised their currency systems at levels at which the internal purchasing power of the currency was substantially in excess of its external purchasing power in order to encourage exports Therefore, "the distribution of foreign trade, which would correspond to the relative efficiencies of different countries for different purposes, has been seriously disturbed from the equilibrium position corresponding to the normal relations between their costs in terms of gold."[1]

But these difficulties arising from the stabilisation of currencies at different levels would have been essentially temporary if the gold standard was allowed to function for a sufficiently long period under appropriate conditions There were other more important complications as well. In the post-war period, the central banks followed a restrictive credit policy Both in France and the United States, there was an aversion towards using the fresh gold acquired in payment of the war debts and reparations for expanding the credit media, and to a large extent gold was simply buried in the vaults of the central banks Notwithstanding the continued inflow of gold, therefore, the price levels in these countries were not only prevented from rising but were actually lowered These measures were fundamentally in contradiction with the gold standard system. The result was a continued pressure on the gold resources of the debtor countries, who were in consequence forced to follow restrictive credit policies Thus, one of the most important principles of the pre-war gold standard, which effected automatic adjustment of exchanges, was not followed during the post-war period

1 Vide Committee on Finance and Industry p 106

Another formidable obstruction in the smooth working of the post war gold standard was the rigidity of the economic structure The integration of industries increase in the strength of trade unions the multiplicity of state controls, heavy governmental indebtedness, etc., created an economic system which was much less capable of adaptations to economic changes than the competitive pre war system—and this at a time when the economic system required greater elasticity than ever before due to more frequent changes in the industrial organisation. A higher standard of living and the emergence of new articles of consumption had changed the character of demand and made it less stable To this elasticity and instability of the demand must be added the tendencies towards growing surplus productive capacity and the flow of numerous inventions This was not all. The price system had become unbalanced and financial structure weakened. In view of all these elements of instability it was imperative that the economic system should be elastic enough to be able to adapt itself to the changes in the environment Unfortunately the system at work was rigid and the rigidity of the price structure made the smooth working of the gold standard extremely difficult

Further the economic system had come to be based on free flow of capital on a large scale This was true both of the manufacturing and the agricultural countries The manufacturing countries had increased their scale of production and they could market their output only so long as foreign capital continued to flow into the agricultural countries This free flow of capital had become a condition essential for the prosperity of the world. Here too the post war conditions were different from those of the pre-war The pre-war financial supremacy of Great Britain was now seriously challenged by the U.S.A. and France In this connection it is significant to note that the American capitalists lacked the experience and traditions which the British financial houses had gained by a long experience Paris was unwiling to lend. The conflicting economic

policies pursued by the three great powers added to the difficulties of the situation

In addition, there were more frequent and large scale movements of short-term capital from one country to another, with changes in economic conditions and confidence, unknown to the pre-war economic system The reserves of gold and foreign exchanges held by the central banks were soon depleted as a result of these sudden flights and led to frightful contraction of credit This maldistribution of gold, was, however, rather a sign of the unhealthy state of the balance of payments due to commercial policy and capital movements and the obligation to repay reparations, than an independent cause of further disturbance

Reparations—Reparations were a constant source of friction between the states during the post-war period and militated against the economic stability According to Herr Salberg, it is in the political payments made from country to country, to an annual amount of two milliards of marks that the final causes of the world crisis lie [1] Up to the end of 1922 Germany paid about 8,000 million gold marks which totally upset her war-exhausted and treaty-depleated economic system The result was a precipitous fall in the value of the Mark and the virtual bankruptcy of Germany In 1923 Germany could not make payments which led to the French occupation of Ruhr To find a solution of this tangle a committee, with General Dawes as the Chairman, was appointed The Committee recommended the stabilisation of the German currency and a graded scale of annuities rising from Rm 1,000 million in the first year to Rm 2,500 million in a standard year This skilful scheme, says Sir Arthur Salter, gave Europe a valuable respite of five years in which she could forget about reparations and proceed with the reconstruction In 1930, however this scheme was superseded by the Young Plan which fixed the payments on a lower scale

1 Vide "World Crisis, Gold Problem and War Debt"

War Debts.—Closely allied to the question of the reparations is the problem of war-debts During the war belligerents borrowed huge sums, both internally and externally, to finance the military operations Taking the external debts contracted during war time, we find that[1] the U K borrowed £842 million from the U S.A , France £1 058 million from the U S.A and the U K., Italy £827 million from the U S.A U K, and France, Russia £766 million from the U S.A , U K. and France, and Belgium £268 million from the U S.A U K and France Other belligerents had also contracted external loans Thus the total value of the inter-allied indebtedness amounted to about £4 000 million These debts were subsequently scaled down and funded In practice, the settlement of these debts depended on the payment of reparations by Germany

That these huge sums were beyond the ability of the war-exhausted and treaty-depleted Germany to pay needs no elaborate proof No wonder, therefore, that even under the Dawes Plan we find that Germany did not make any net payments[2] During 1925 29 Germany's external loans amounted to £3,540 million and reparation payments to £1,985 million[3] This increased Germany's dependence on foreign loans Further, the protectionist tariff policy pursued by the U S.A and France made it impossible for Germany to pay the debts, even if she had a desire to do so Again, the pre-war foreign investments were gradual and regular, which enabled the countries to adjust their economic systems to this continuous movement of capital The post-war movements of capital, on the contrary, were most erratic Again, in the post-war years lending and borrowing were reckless, extravagant and wasteful The absence of a strong central agency to regulate the world money market in the post-war period

1 Keynes, J M "Essays in Persuasion," p 31

2. Imports of capital exceeded Germany's payments to foreigners on account of interest and reparations by a considerable sum, which was balanced by large net imports of merchandise gold, and foreign exchange

3 Balances of Payments (League of Nations), 1932-33, pp 8 and 15.

added to the difficulties The blame, therefore, largely rests with the creditor countries

Foreign Investments—In the pre-war days foreign loans assisted the growth of world trade and commerce bec the borrowings were primarily for productive purposes the creditor countries utilised their receipts either for purchase of goods and services from the debtor countries for making additional loans, it being accepted that all lo must ultimately be paid in goods and services This ma the payment of capital and interest relatively easy and tl whole mechanism worked without friction The Great Wa changed the entire economic outlook of the people anc created fresh complications Firstly, the post-war loans[1] were largely of an unproductive character, having been incurred either for political purposes, or to support exchanges or to build up currency reserves or to balance the budgets The ability of the debtor countries to pay these loans was, therefore, considerably restricted In consequence the debts piled up and further increased the difficulties of the debtors To this must be added the reluctance of the creditor countries to receive interest and amortisation charges in the form of goods and services The demand was for gold or short-term liquid assets This the debtor countries could not do For a time the creditor countries went on giving fresh loans to meet the situation But the most serious error on the part of the creditor countries was their refusal to receive payments in the form of goods and services [2] The dangers of the situation they had created were brought home to them when they stopped lending

1 A large part of the responsibility for disasters that have overtaken the intern loans of the post war period is undoubtedly attributable to the recklessness and lack crimination with which many of these loans were made It would be superficial how to assign the whole responsibility to such causes Many of the loans which in the light of our after knowledge seem imprudent to the point of recklessness did not seem so even to cautious observers in the atmosphere of the post war decade For a complete diagnosis of the trouble it is necessary to take into consideration factors of a more fundamental character Vide "The Problem of International Investment, p 12

2 The heart of the problem was the difficulty of transfer To meet the service of her external borrowings it was not enough for Germany to produce additional goods to the required value She must market those additional goods in world markets and thereby obtain foreign exchange Equally for the United States to receive payment it was necessary that America should import additional goods from outside world or else reduce her exports by a corresponding amount Vide The Problem of International Investment p 13

This is not all. In the pre-war days loans were advanced by the industrially advanced countries to relatively backward agricultural countries, which facilitated smooth functioning of the economic system. In the post-war period, however, loan transactions were largely entered into between the advanced industrialised countries, which increased the difficulties of payment.

Short-term Capital Movements.—Here we have another cause of economic instability In the pre-war days the short-term capital movements rendered an invaluable service in adjusting the balance of international payments, because the total amount of such sums was relatively small and they were largely controlled by the London money market. In the post-war period, however the volume of short-term capital movement increased considerably due inter alia, to political uncertainties, instability of the currency systems and a high rate of interest on the short-term loans. The sudden movements of these huge amounts from one country to another, characteristic of the post-war period, became a formidable source of economic instability. The insecurity of the position was increased by the fact that the very countries whose credit was likely to be most affected by political changes had incurred foreign indebtedness, of a short-term character on a very large scale. Germany had borrowed no less than Rm 11,200 million to Rm. 12,200 million or $2 600 million to $2,900 million on a short-term basis. The existence of such borrowings increased the vulnerability of the international financial position particularly of countries likely to be hard hit by the depression or subject to considerable withdrawals of foreign short-term capital.[1]

Protectionist Tariff Policy.—Before the World War international trade was regulated primarily by customs duties and the balance of payments was left to be adjusted by the international monetary and credit system. Judged by the post-war standards, the degree of protection was

1. Vide, Course and Phases of the World Economic Depression, p. 56.

relatively moderate. Besides, the highly intergrated international trade, monetary, and credit systems imparted relative stability to the entire economic system. These systems were completely disrupted by the War and its aftermath. No doubt the systems were rebuilt during the first post-war decade, but the basis on which the new superstructure was raised, was essentially unsound and led to far more drastic and extensive protectionism than that of the pre-war period. The problem of direct adjustment of balance of payments was also brought to the fore. Both these forms of protection became more and more intensified as the economic depression unfolded itself.

Distorted Price Levels.—The rapid rise in the efficiency of both agriculture and manufacturing industries considerably increased the per capita output in all the advanced countries. Under normal conditions, this efficiency ought to have inevitably led to a reduction in the price level. But the monetary policies pursued during 1925-29 distorted the entire price structure. During 1925-27 the wholesale price level fell in conformity with the improved efficiency in the technique of production. This tendency, however was abruptly arrested in 1927, due to the cheap money policy initiated by the United States, to relieve the domestic depression and check the drain of gold. This inflationary policy created disequilibria in the economic systems of the world, which eventually produced the slump. The cheaper credit policy of the United State, by making possible similar policies in other countries, and also by providing a means of interest payments in the shape of new loans enabled the debtor countries to maintain wage levels and standards of living that would have been impossible without such support.[1]

The credit expansion, which took place during this period in the United States, was largely for the financing of speculation, which had dangerous consequences. In view of the marked growth in business profits and the enormous

1 Vide, World Economic Survey 1931-32 p. 53

inflation in share prices, the average American investor found it more profitable to invest his capital in local shares than in subscribing to the foreign loans The result was a substantial fall in the foreign loans, which upset the economic structure of the debtor countries They were forced to follow "dear' money policy which led to falling prices, lower output, and unemployment This state of affairs was essentially short-lived The fall of this artificial system was inevitable and it came with the collapse of Wall Street in October 1929 plunging the world in an unprecedented economic depression

Depression —During the depression the economic trends outlined above were intensified It has been rightly asserted that the depression exposed the unsoundness not only of the economic system which had been built up after the war, but its political basis as well, and caused economic distress and economic friction to coalesce We have already noted that the economic system was overburdened with excessive financial commitments, large proportion being unproductive, and its important segments had become rigid, they were not amenable to an easy control The Wall Street crash gave a rude shock to business confidence and was followed by a steep fall in the inflated paper values Banks promptly recalled their advances and curtailed their credit facilities These measures had a deflationary effect and prices slumped

In all such cases of a steep fall in prices, the first loss falls upon the profits of industry, which are curtailed or entirely wiped out As a result, enterprise and investment are discouraged, industrial production is curtailed and unemployment follows Besides, once a decline in prices sets in further decline is expected The incentive both to spend and invest is weakened Uncertainty and insecurity ensue, leading quickly to the undermining of confidence Potential purchasers await the expected fall and, by awaiting, help to cause it Production is paralysed, unemployment increases and a vicious downward spiral is set in motion [1]

[1] Vide Report of the Gold Delegation Para 145

The effects of this slump in prices upon different economic systems were essentially dissimilar The policies pursued by the advanced countries to protect their economic systems during the trough of depression have considerably complicated the technique of protection In fact, the entire technique of protection was revolutionised In several cases there were distinct innovations and in others the scope and effectiveness of the old devices was remarkably extended In what follows, therefore, an attempt will be made to present, in brief, the salient features of the different forms of protectionism, their nature, and the objectives they are designed to serve

From the preceding discussion it will be seen that due to faulty economic policies pursued by different countries it was inevitable that the system resting upon them must crash When the inevitable crash came its repercussions were, therefore, widespread The industrial depression set in simultaneously with the agricultural crisis and their interaction added to the intensity This led to a steep fall in the prices of primary commodities, which reduced substantially the real incomes of the agricultural states, increased the real burden of their debts, and adversely affected their credit The balance of international payments was adversely affected due to the fall in the value of exports and the contraction of the foreign credits The economic conditions of these countries were particularly serious due to the peculiarities of their economic systems Besides, they were heavily in debt, the loans having been contracted at high rates of interest and partly for unproductive purposes They had also "valorised" their agricultural products by accumulating stocks No wonder therefore, that the rapid fall in prices upset their entire economic system

Thus, these countries were faced with an extremely difficult situation The difficulties were two-fold, external and internal Attemps were made to solve internal difficulties by extending protection to agricultural interests in the

country adversely affected by the steep fall in prices The failures of schemes intended to stabilise agricultural prices led to a further price instability The internal taxation was also raised to improve the situation These policies exercised a deflationary effect and forced down the prices still further [1]

The external problem was equally serious and difficult To meet their external obligations adequately and promptly, the agricultural debtor countries tried to cut down their imports But these experiments had very limited success This was so because the prices of agricultural products, which constituted the means of payments to the creditor both in respect of their debt obligations and of imports, had fallen much lower than those of industrial products which formed the bulk of their imports Further, the creditor countries had abruptly cut off their foreign loans and imposed protective tariffs on the imports of agricultural produce, to foster the growth of agriculture within their own frontiers Under the circumstances, the agricultural debtor countries had three alternatives (1) abandonment of the gold standard, (2) export of gold, and (3) proclamation of moratoria All these alternatives were tried, but they failed to arrest the fall in prices

Protectionism—Agricultural protectionism of the advanced industrial states is of special significance in the technique of modern commercial policy, which the present work attempts to analyse We have already noted that the agricultural debtor countries, to safeguard their balance of payments, had resorted to a ruthless cut in their imports These import restrictions increased the difficulties of advanced industrialised countries, their exports dwindled and unemployment increased Besides, the general protectionist policy, which was gaining ground throughout the world, further aggravated the export difficulties At this

1 A fall sometimes catastrophic spread with extreme violence to almost all agricultural produce It was so rapid that by the end of the year while some products reached pre-war level of prices others fell as low as one quarter or one-half below the 1913 level In many countries the fall in agricultural prices was the most abrupt experienced for half a century and save for the period 1920-21 the modern economic history gives few instances of such a decline Vide Agricultural Crisis Vol I p 8

stage, the industrial countries, which were normally importers of agricultural commodities, took special measures to protect their agricultural population by imposing tariffs, milling regulations, subsidies, import licenses, quotas, monopolies, sanitary regulations, etc All these measures were extensively used and often abused "These Draconian measures, which, quite apart from the disorder which they caused in the delicate and complex mechanism of the balance of international accounts, tend to create as many different price regimes as there are protectionist countries and thus delay a return to the essential system of non-watertight compartments, were followed by a whole series of difficulties, perhaps less serious but almost as irksome Quotas have to be allocated as between the countries; hence the danger of discrimination Quotas have to be allocated as between the traders, and allocation is necessarily synonymous with delay, confusion, abuse, de facto monopoly and sometimes corruption The whole body of sanitary measures, applied with the utmost severity, creates a suspicion that those measures have economic objects "[1]

Agricultural protectionism within reasonable limits is defensible The costs involved in a reasonable protective scheme may be more than counterbalanced by the benefits derived therefrom Apart from the modern tendency towards economic self-sufficiency, the recent experience of the depression has shown that an over-industrialised system is more vulnerable to economic disequilibrium Therefore, a more broad-based economic system is preferable Besides, the maintenance of a healthy agricultural population due to social, historical and psychological reasons, has come to be regarded much more important than pure economic considerations would permit

The agricultural protectionism during the post-war period has overstepped the reasonable and defensible limits In the preceding chapter we bave shown that agricultural

1 Vide Report on Agricultural Protectionism, (League of Nations) p 6

protection became an important instrument of commercial policy in the nineteenth century. This trend became particularly marked after 1878. The financial needs of balancing the budgets by customs revenue increased the popularity of tariff protection. Since protection breeds protection, each time a tariff was revised heavier duties were imposed. Gradually, the technique of protectionism was improved. Tariff specialisation increased the efficiency and effectiveness of protectionist policy. But it is essential to note that customs duties were the primary instrument of protectionist commercial policy before the Great War.

For a few years following the Great War, the tariff policy affecting the agricultural products was relatively liberal. This change in the trend towards agricultural protection was due to scarcity of foodstuffs and raw materials. In consequence, the volume of world trade in some of the chief foodstuffs was considerably greater after the war than before it. The world exports of wheat and wheat-floor, for example, increased by about 18 per cent in volume between 1909-13 and 1922-25, the European import balance rising by more than 20 per cent, if Russia is excluded, and by about 90 per cent if Russia is included. The total of the import balances of beef and veal into five of the leading European importing countries was twice as large in 1925 as in 1909-13[1]

This period of relatively liberal tariff policy was cut short in 1925. Since then the customs duties on agricultural products have been rising in industrial countries. In 1925, the Italian Government re-imposed customs duty on wheat, which had been abolished in 1921, and inaugurated its wheat-growing campaign, with the intention of minimising Italy's dependence on foreign food-supplies. Austria and Czechoslovakia also imposed sliding scale duties on the imports of wheat. Germany, having recovered her freedom to impose customs duties, followed the lead. Duties on meat also showed a rising tendency during this

1 Vide, Report on Agricultural Protectionism (League of Nations) p 29

period The German duty on fresh and chilled meat was raised in 1927 from 21 Rm per 100 kg to 32 Rm Similarly, French duties on beef were raised during 1927 from 50 to 350 francs per 100 kg on fresh and chilled beef and from 50 to 180 francs in the case of frozen beef

The period of world depression since 1929 is very significant in the technique of commercial policy The innovations made during this period show the extent to which human ingenuity can go in devising fresh expedients to meet new situations This period has recorded marked changes in both agricultural and industrial protectionism The principal changes in the technique of commercial policy during this period may be studied under convenient heads

(1) **Customs Duties: America**—Apart from a few sporadic changes in customs duties affecting some individual articles the first important general increase in duties was effected by the United States under the Hawley-Smoot Tariff Act of 1930 Under the Act the tariff duties were raised both on agricultural commodities and manufactured goods Sugar duty, which had played a very important part in the American protective tariff, was raised from 1 76 cents per pound to 2 00 cents, although there was no change in the difference in costs and prices during the period Thus the cost principle did not warrant the imposition of a higher duty Similar was the practice followed *in respect of other agricultural articles* On wheat a duty of 20 cents a bushel was levied in 1922 and was then thought to be too high This duty was raised to 42 cents a bushel in 1924 and was maintained at that height under the Act of 1930 On long staple cotton duty of seven cents a pound was imposed to help the cotton growers On beef the duty was raised from 3 cents to 6 cents, on sheep from 2½ to 5 cents, on mutton and lamb from 4 to 7 cents and on swine from ½ to 2 cents On milk and cream the duties were nearly tripled, and on live poultry the increase was from 3 cents to 8 cents The duties on eggs and butter

	Act of 1922 Per Cent	Act of 1930 Per Cent.
Spirits, Wines and other beverages	36 48	47·44
Manufactures of Cotton	40 27	46 42
Flax, Hemp, Jute and manufactures of .	18 16	19·14
Wool and Manufactures of	49 54	59 83
Manufactures of Silk	56 56	59 13
Manufactures of Rayon	52 68	53 62
Paper and Books	24 72	26 06
Sundries	21 97	27 39

The Hawley-Smoot tariff had very important repercussions it revolutionised the commercial policy of the world In the initial stages it led to widespread retaliation and discrimination against American exports but soon developed into a network of restrictive tariffs This was not all In addition to the general increases in protective tariffs we find a system of import and export restrictions unknown in the pre-war days, which made the movement of goods from one country to another extremely difficult We have already pointed out that the normal working of the gold standard tends to correct the balance of trade when necessary by increasing the imports of the creditor countries The gold standard will perform the function of automatic adjustment of trade balance even if there is a permanent tariff, though with some difficulty But the adjustment becomes impossible if the flow of imports, which the normal working of the gold standard requires, is obstructed by higher and restrictive import duties The new American tariff definitely and deliberately kept the imports out of the American markets, which her creditor position required her to receive Under these circumstances, with the commodity-prices falling rapidly, with new loans unavailable, a retaliation was inevitable and logical The retaliatory or "defensive" tariffs were erected in many countries in desperate efforts to create export balances for the debt-payments and to check the price-declines, and the depression continued rapidly in its des-

cending vicious circle[1] No wonder therefore that the world commercial policy since 1930 shorn of its normal features has assumed a chaotic form.

Italian Tariff Policy.—All European countries immediately started raising their tariffs The Italians said that they would make purchases only in those countries which bought Italian agricultural products marble cars ships silk, wool and cotton manufactures This declaration was followed by the new automobile tariff in June 1930 which was prohibitive in its effects "Practically all agencies handling American cars had been liquidated by November 1930 dealers finding themselves not only unable to sell automobiles at the new rate but unable to get rid of the stocks acquired under the old rates due to the fact that the Italians would not purchase automobiles which would soon be left without service facilities and parts."[2] In defence of the new policy it was stated that the increased duties assessed by the Italian Government constituted an effort to conserve the national industry and to relieve unemployment. This increase was a part of the established protective tariff policy to conserve national industries. In September 1931 the tariff duties on radios and radio equipment were raised. Further at the same time a general 15 per cent. ad valorem increase in tariffs on all products imported into Italy was effected, save a few specifically exempted articles like wheat corn, bread, metal ores chemical fertilisers coal coke etc This measure was taken to balance the budget The intensification of depression all over the world including Italy the fall in prices, and the excessive tariff barriers raised by almost all countries had cut down production, consumption and exportation, and thus had reduced revenue These measures, in addition to the attempts made by the Italian Government to restrict imports had curtailed considerably the customs receipts Internal taxation had reached the point of diminishing returns It was believed, therefore that the best method of

1 Vide, Jones, J M. "Tariff Retaliation," p. 11.
2. Vide Jones, J M. "Tariff Retaliation," p. 22.

securing more revenue was to raise the tariffs generally The result was that by 1931 Italy exceeded all industrial countries in Europe in the height of her tariff walls [1] The duties on agricultural products were also increased particularly on corn, flour and sugar In 1932, duties were raised on butter, livestock and meat

German Tariff Policy—The agrarian protection has played an important part in German tariff policy, since Germany regained her commercial freedom on the 1st January 1925 The tariff Act of August 1925 introduced moderate protectionism During 1925-26 several revisions were effected in the tariff rates so that by 1927 they had risen by about 55 to 65 per cent above those of 1913 The increases were more significant in the case of vegetables, fruits and dairy produce cocoa, etc During 1929 and 1930 sliding scale of duties were enforced to keep the home price at a definite level Since then these rates have recorded a rapid rise with the fall in prices For instance, the duty on wheat rose from 65 Rm per ton in 1929 to 250 Rm in 1931, on rye from 60 Rm to 200 Rm, on barley from about 40 Rm to 200 Rm and on wheat floor from 102 Rm to 430 Rm [2] These duties were supplemented by compulsory milling regulations The most obvious effect was practical exclusion of all imports of wheat and rye With regard to maize, a selling monopoly was established in 1930 which completely stopped the imports Therefore, the German imports of grain which constituted 10 4 per cent of the total German imports in 1913 fell to 4 4 per cent in 1931 [3]

Protection to live-stock breeding and meat production was also substantially increased In 1931 the duties in force were about four fold of those in 1913 The duties on meat were correspondingly raised In consequence imports of live-stock declined from Rm 78 million in 1929 to Rm 2 2 million in 1931, and those of fresh meat from Rm 22 4

1 Vide Liepmann H "Tariff Levels and the Economic Unity of Europe pp 69 73
2 Vide Liepmann p 60
3 Vide Liepmann, p 61

to Rm 5 5 million Since 1932 the tariff duties have been supplemented by quotas monopoly, etc As a result of this development by the end of 1931 Germany had become nearly self-sufficient in wheat and rye and requirements of grain and fodder were small, imports of live-stock and meat were reduced to insignificance, while some sugar supplies were sufficient to meet the entire home demand

Industrial duties could not be increased because they were tied by the commercial treaties Besides, Germany being a large exporter of the manufactured goods could not afford to raise her tariff such as would invite retaliation The excessive agricultural protection adopted by Germany had already created sufficient difficulties for her exports which had to be solved by suitable commercial treaties [1]

French Tariff Policy—The pre-war French agrarian tariff was decidedly protectionist The tariff revision of 1927 brought down the level of tariffs considerably and stabilised it by negotiating commercial treaties In 1929 however these duties were altered Those duties which were not consolidated by commercial treaties were raised particularly those on corn flour, live stock, meat and milk products sugar and wine The incidence of duties was much higher in the case of those commodities the prices of which had fallen very heavily Thus, the duties were very high on wheat maize barley, pork, sugar etc The tariffs were supplemented by milling regulations and quotas, which we shall discuss at a later stage

As regards the industrial tariff in France it has been pointed out that the tariff revision of 1927 and the commercial treaties concluded thereafter had consolidated the tariff With the inception of depression and the steep fall

1 " German policy in this matter is to become self sufficing in those food-stuffs and raw materials for which she has an inelastic demand or which, if they were cut off in the case of war or as a means of political or economic pressure in time of peace would bring disaster to the State There is, however general agreement in Germany that it is not desired, even were it feasible to make the country completely self-sufficing so that she ceased to have any foreign trade The utmost importance is attached to increasing the volume of German exports, in order to make it possible for her to raise the standard of living of her people by increasing her imports, subject to the general proviso that these imports should be of a type which could be dispensed with in time of war without endangering the security of the Country " Vide Guillebaud, C. W Economic Recovery of Germany p. 2?9

in prices, therefore, French trade and commerce could not easily seek the assistance of tariffs A few increases were effected up to 1931 but they were inadequate to render any material assistance In 1932 quotas were, therefore, introduced to rectify the balance of trade and protect the French industries by cutting down drastically both the agrarian and industrial imports

Britain adopts Protection.—At the general election in 1931, the National Government, in view of the rank protectionist policy and the other import restrictions adopted by the leading industrial countries, obtained a mandate for the defence of the British market The protectionists argued Great Britain must have a tariff, as a means of defence to retaliate against countries which persisted in excluding the British products in order to be able to reduce foreign tariffs which were strangling British trade, and to prevent state-aided foreign products from being dumped in Great Britain, at prices disastrous for the British industries The British people were told, and believed, that in a world of vicious and prohibitive trade restrictions, Great Britain could not survive as a free market and that the only way in which Britain might secure freer trade and lower tariffs throughout the world was for her to adopt protection as a bargaining weapon

In accordance with this definite change in the British tariff policy, the Abnormal Importations Act was passed in 1931, which empowered the Board of Trade with the concurrence of the Treasury, to assess customs duties up to 100 per cent ad valorem upon the manufactured goods when necessary to prevent abnormal importation of goods which were being brought in for the purpose of forestalling the permanent tariff measures then in course of preparation Three Orders issued under this Act, in 1931, comprised a long list of articles, and the duties imposed were 50 per cent ad valorem, with exemption for Empire products

The Horticultural Products Act of 1931, soon followed, which empowered the Minister of Agriculture to impose

duties not exceeding 100 per cent ad valorem upon certain fresh fruits, fresh vegetables, flowers, plants, bulbs, and foliage, and to reduce the importation of those commodities, the production of which can be increased in the U K, or which can properly be regarded as articles of luxury

In March 1932 the Import Duties Act came into force, imposing a general ad valorem duty of 10 per cent on all goods imported into the U K, except certain goods The exempted articles were the raw materials used by the British industries, e g, cotton wool, hides and skins, metallic ores, tea, rubber, etc as well as certain food-stuffs, including wheat, maize pears, live animals, etc The Act also provided for the constitution of a Committee, to be known as the Import Duties Advisory Committee for advising the Treasury regarding (a) any additional duty that should be imposed on goods chargeable with the general duty which are either articles of luxury or of a kind which are being produced or are likely within a reasonable time to be poduced, in the U K in quantities which are substantial in relation to the U K consumption, (b) additions to the list of goods to be exempted from the ad valorem duty, (c) the allowance of drawback of duty on any class of goods The Committee is further directed to have regard to the advisability in the national interest of restricting imports into the U K, and in the interests generally of trade and industry in the U K

This measure was highly commended by Mr Chamberlain He claimed that it would help to correct the balance of payments by diminishing imports and stimulating exports, fortify the finances of the country by raising fresh revenue, and effect an insurance against a rise in the cost of living resulting from an unchecked depreciation of currency It would decrease unemployment by giving the necessary stimulus to industry and agriculture Further, it would be used as an instrument of tariff bargaining, to lower tariff barriers in the foreign countries Cementing of the ties between the Empire was another objective aimed at

The Import Duties Advisory Committee has rendered very useful services to the British trade and industries It has issued a series of reports The first report, issued in April 1932, is most interesting and comprehensive It recommended the levy of uniform rates of duty on fully manufactured articles and higher rates on luxury and semi-luxury articles These rates could be lowered or raised in individual cases on the basis of detailed investigations From time to time changes in rates of duty on various commodities have been made on the recommendation of the Committee Everybody has a right to apply to the Committee, for the revision of the duties, and all interested parties are invited to express their views

Before the end of 1932 came the Ottawa Agreements Act, which gave a more definite orientation to the post-war changes in the British tariff policy and clarified their objective The exemption accorded to the Empire products under the Import Duties Act of 1932 was extended for a further period of five years Great Britain undertook to pass legislation levying, for the purpose of enlarging the Imperial Preferance, new duties on certain imports from foreign countries, previously admitted free, and to increase the rates of duty on certain foreign imports previously admitted with a duty of 10 per cent *ad valorem* Wheat, maize, linseed, and copper were taken out from the free list and specific duties imposed upon them The 10 per cent duties previously charged on a large range of fresh, canned, and dried fruits, dairy products, cereals, fresh and canned fish, eggs, honey, vegetable oils, rice etc, were replaced by specific duties which constituted increases from 33-1/3 to 100 per cent This was not enough Great Britain undertook to restrict importation of foreign chilled and frozen beef, frozen mutton and lamb, as well as bacon and ham, by means of a quota system, with the object of securing the development of home production and giving the dominions an expanding share of the British imports Further, Great Britain agreed that upon a long list of

foreign imports, the existing 10 per cent. duties would not be decreased for a period of five years

From the foregoing brief review of the tariff policy of a few advanced industrialised countries during the depression it will be seen that the customs duties play a very important part in the technique of modern commercial policy This is a universal practice But it has also been found that the customs duties are not sufficient to provide adequate safeguard to trade and industries suffering from the steep fall in prices and shrinkage in demand It is significant to note that higher customs duties on agricultural produce in advanced industrial countries aggravated the difficulties by reducing the capacity of agricultural countries to buy manufactured goods 'Profit deflation" affected adversely the capacity and willingness to lend abroad The result was that tariff duties have been supplemented by other devices

(2) **Currency Depreciation.**—It has already been pointed out that in 1925, when Brtain reintroduced gold standard, the pound was over-valued by about 10 per cent It was expected that a rise in prices would bring about the necessary adjustment But the general trend in prices since 1925 has been downward, which affected British trade and commerce adversely The difficulties were aggravated because some other important countries had returned to gold at rates relatively under valued, to offer a definite encouragement to their trade and industries France was the leader of this group The British balance of payments could be maintained with the help of receipts from external investments, shipping, etc In 1931, however, the balance became heavily unfavourable and imposed a severe strain upon sterling, confidence in sterling was lost There was a run on the pound during the summer of 1931 and in about two months' time more than £200 million of gold was withdrawn Short term loans were borrowed from Paris and New York to support the sterling, but the drain continued with the result that in

September 1931 Britain left the gold standard Since then sterling has been a managed paper standard The depreciation of sterling was definitely helpful to the British manufacturers, British trade and industries got a substantial stimulus The trade balance recorded immediate improvement The British lead was soon followed by other countries, so that the currency depreciation became an important instrument of commercial policy soon after September 1931

An immediate result of currency depreciation is to improve the competitive capacity of the domestic producer both in the domestic and the foreign markets This advantage however tends to be nullified because depreciation induces a rise in the domestic prices Besides the exchange depreciation is not favoured by the foreign competitors, who regard it as an unfair competition This is so because when a currency is undergoing depreciation normally the decline in its internal purchasing power lags behind the decline in its external purchasing power as measured by the foreign exchanges A depreciated currency, therefore, tends to operate as a premium on exports by causing export prices, temporarily at least, to be abnormally low in terms of the foreign currency The competing countries, adversely affected by the currency depreciation either follow a similar course of action or impose countervailing import duties or other special restrictive measures Thus, the commercial advantage of currency depreciation tends to be neutralised But it creates considerable complications in the commercial policy and leaves an heritage of dangerous restrictive commercial practices

(3) **Quotas** —The quota system has been adopted to meet new conditions of trade, where customs duties have failed to provide adequate protection to the domestic producers Under the quota system, the amount of a particular commodity which may be imported into a country during a specified period is fixed, usually in advance We may define the quota system as limitation by quantity or value of the importation of a commodity for a specified

period of time by the executive decree of a State The quota may be allocated between the supplying countries or it may be unallocated. When the quota is unallocated among the supplying countries, the importing country does not take cognisance of the origin of imports, and permits the imports to flow in until the quota has been filled in Thereafter imports are prohibited When the quota is allocated among the supplying countries each country may supply its permitted share at any time during the quota period

It is, however, essential to note the distinction between an import quota and a *customs* or *tariff* quota Under the import quota the physical quantity of imports during *a specified period is fixed, nothing beyond that quantity* shall be imported But, under the customs or tariff quota, *a fixed quantity of imports can enter at a certain concession* rate of duty, and imports above that quantity would *have to pay the higher rates of* duty *Thus, in this case* imports are not legally prohibited, but they are subjected *to higher customs duties*

The quotas have marked effects on the balance of payments, as distinct from the customs duties A customs duty raises the prices of commodities to the consumers, since it operates as a form of tax to enable the domestic industry to sell at a higher price But this does not eliminate the foreign competition entirely Of course, the foreign competitors at the margin may be eliminated, in view of the higher price, and the margin for the domestic producer may widen But, if the customs duties are not prohibitive, the foreign imports will continue to flow in and keep the domestic producers alert No wonder, therefore, that so long as the customs duties continued to be the primary instrument of commercial policy, foreign trade recorded a steady growth, notwithstanding the increase in duties The machinery for maintaining the equilibrium of the balance of payments was maintained intact

Under the quota system, however, the imports are regulated more effectively by imposing a quantitative

limitation upon them, and the foreign competitor has no freedom of increasing his sales at competitive prices He can export only so much and no more Under a reasonable customs tariff, on the other hand, the foreign manufacturer has always a possibility of maintaining his sales by improving his technique of production or acceptance of a lower remuneration

Again, the quota system, by making the goods scarce in the domestic market, imposes very severe strains upon the price mechanism and makes the re-establishment of price equilibrium more difficult The price variations differ with the stringency of the application of the quotas Prohibitive duties may bring about similar results, by imposing pressure upon the price level, but the process is apt to be dilatory and not so rigid

The quotas are fixed by the executive authority, and therefore they are apt to reflect more the caprices and the needs of those in power than the requirements of the large mass of people Thus under the quota system the administrative authorities have acquired a greater measure of power in moulding the commercial policy than they could have under the customs duties determined by the legislature It is claimed that the quota system is more flexible and can be promptly adjusted to suit the changes in the economic conditions without having a recourse to dilatory legislative practice It is easier to manipulate a quota than mould a customs duty But this practice has its own dangers Quotas must of necessity be allocated, and allocation is synonymous with delay, confusion, error, abuse, *de facto* monopoly, and at times corruption Further, the quotas can be more promptly enforced without the obstruction of the dilatory tactics of the legislators The danger, however, is that since the authority imposing the quota is not bound to disclose and defend its policy before the legislature, the much needed check on the caprices of the authority is removed, which does not savour well for democratic conditions Again, import quotas are likely to escape public criticism more conveniently than customs

duties, because the public gets more conscious of the burden of customs duties than of import quotas Thus, quotas are more suited to economic and political expediency In commercial bargaining as well, quotas are more useful in securing concessions from the other countries than customs duties, because of their greater effectiveness in excluding the imports At the same time, it is easier in the course of negotiations to increase a quota than to reduce a duty Above all, quotas can be used without infringing the letter of the obligations entered into under commercial treaties incorporating the Most Favoured Nation Clause This exclusion of the quota system from the ambit of the Clause has led to unlimited discrimination and neutralised considerably the efficacy of the Most Favoured Nation Clause

France gave the lead by adopting the quota system as an instrument of commercial policy in 1931 The chief objects of the French customs quota policy were First, to protect the national market from ruinous importation, to reserve the national market to national production, and to redress the deficitory trade balance, and second, to create a barrier against importation behind which the Government could proceed with the denunciation of France's most-favoured-nation treaties, to secure tariff liberty, and to proceed with the negotiation of new treaties strictly on the basis of reciprocal concessions, abandoning the unconditional Most-Favoured-Nation-Clause With these objects in view, France placed the import of coal on a quota basis in 1931 Thereafter followed a rapid succession of decrees restricting the importation of raw materials and foodstuffs, flax, wines, woods, animals and meats, chemical fertilisers, fish, poultry and eggs, furniture and brooms, natural flowers, ham and milk, chicory and chicory roots, sugar, bananas, and canned fish In 1932 the restrictions appeared on the manufactured products, which covered 1,131 items,

or one-seventh of the total list of products covered by the French tariff, upon their importation into France Since then the system has gradually widened its scope and increased in its rigidity The French example was followed by a number of advanced countries with the result that quotas are today the most common feature of modern commercial policy Britain, too, adopted the quota system

(4) **Exchange Control**—*The currency instability led to* further developments in the technique of modern commercial policy The causes which led to the breakdown of the international monetary system have been noted Monetary depreciation, initiated to protect the national economic systems from the trough of depression, in effect added to its intensity, and led to innovations in the technique of commercial policy which not merely prolonged the depression but have endangered the very structure of the modern industry and commerce Faced with a progressive and dangerous depletion of their stocks of foreign exchange, some countries, afraid of depreciating their currencies, felt that the only way by which they could safeguard their currency systems was to limit, and if need be even suspend transfers abroad on account of financial obligations and also to place restrictions on the purchase of foreign exchange required to pay for the imports Thus, the objects of exchange control were twofold, the protection of national currencies from the strain of the external balances of payments and safeguarding the domestic trade and industries from extraordinary price cutting and exchange dumping

Foreign exchange control, therefore, became an important and common instrument of commercial policy Under this system, the Central Bank is authorised to impound the foreign exchange derived from export receipts Provision is made whereby the receipts from exports must be deposited with the Central Bank, which has also the power to mobilise foreign exchange derived from other sources Payment for imports is thereafter possible, theoretically,

only by obtaining the requisite foreign exchange from the Central Bank. Thus, the Central Bink is able to control the external drain upon its reserves and maintain the external parity of the national currency

The use of exchange control has led to the system of double or multiple money[1] This is so because in some countries the Central Banks were not able to control the market effectively and led to the growth of 'block' markets in which the national currenry exchanges at depreciated levels The mark, the peso, the pengo, or the lira, for example, have a qualifying prefix Tourist marks are quite familiar Similarly, there are many varieties of currency in different countries with varying external, but uniform domestic purchasing power The rates of exchange depend upon the amount of foreign exchange available and the purpose for which they are required.

Clearing and Compensation Agreements.—Exchange control begets clearing and compensation agreements We have already noted the tendency of "block" markets to develop under the system of exchange control The difficulties created by exchange control in getting adequate and prompt foreign exchange to finance foreign trade transactions have led to agreements between state organisations or private enterprises for barter trade transactions without the use of credit

The clearing agreements entered into between the States consist of arrangements whereby a central authority (usually the Central Bank) in each of the contracting countries concerned receives payment for imports from, and disburses payment for exports to, the other country The accounts in each country are balanced in an agreed proportion Thus, the primary intention with which these agreements are entered into is to regulate the trade on a bilateral basis so as to decrease passive balances and to bring about an equality between imports and exports In recent years these agreements have multiplied rapidly.

1 Vide World Economic Survey, 1932-33

Compensation agreements have also become more common The difference between the clearing and compensation agreements need not be overstated, and in practice the tendency has been at times for the two systems to merge into one The clearing agreements do not specify, as a general rule the barter of particular commodities, but allow the trade to be regulated, within certain limits, by the ordinary commercial channels[1] The limits have been stated in the preceding paragraph The compensation agreements, on the other hand, specify the quantity of the goods to be exchanged and the time within which the exchange is to take effect For instance the Turkish Ministry of Exchange and an Austrian Tobacco Company entered into an agreement in November 1932, by which the Company agreed to buy, up to the end of June 1933, Turkish tobacco to the value of 20 million French francs, payable in Austrian merchandise The Swedish Government made a similar arrangement with Greece to import tobacco to the value of $400 000, 20 per cent of which sum was to be written off the Greek debts in Sweden the remaining 80 per cent being paid for in Swedish goods Similarly, we have the compensation agreement between Hungary and Czechoslovakia of December 1932, by which 29,000 Hungarian pigs are to be exchanged for 20 000 wagons of Czechoslovak wood fuel, and Hungarian eggs and similar products to the value 1½ million crowns are to be paid for facilities accorded to Hungarian tourists in the Czechoslovak thermal stations

The clearing and compensation agreements have caused serious damage to the international trade By directing the flow of international trade into rigid and narrow bilateral channels, they have prevented regional specialisation and the most efficient use of national resources Under normal conditons, international trade is polygonal Further, as a result of these clearing agreements the direct balancing of trade between two countries concerned is effected by an ever-increasing restriction of international

1 Vide World Economic Survey 1932 33

trade Under such a system international trade will continue to suffer

(5) **Subsidies and Measures Incidental thereto.**—Subsidies have come to play a very important part in the technique of modern commercial policy particularly since the depression It has already been pointed out that since the depression serious attempts have been made to encourage domestic industries Of the different devices used to stimulate internal industrial expansion, subsidies are very important These subsidies or bounties consist of various kinds of payments or other benefits granted either by the State or private organisations upon the production or exportation of specified articles, thus placing the subsidised industry or export branch in a more favourable position as compared with other similar national or foreign industries or export branches Thus, the intention in making use of this device is to improve the competitive position of the favoured producer or exporter as against other producers

The subsidies may be direct, in the form of outright cash grants to the producers or exporters, or indirect, in the form of remission of taxes, drawbacks of various sorts, etc The direct subsidies may be (1) governmental or (2) private export bounties The direct Government subsidies are very common To illustrate from the British Governmental practice, we find the most conspicuous case of British beet sugar subsidy In the post-war period, the first important step in public assistance was taken by the British Government in 1922, on the plea of reducing the country's dependence on overseas sugar supplies, of mitigating agricultural unemployment, and of improving the soil for cereal crops. Accordingly, the excise duty on sugar produced from homegrown beet was abolished This measure proved inadequate to encourage rapid expansion, and hence in 1925 a subsidy was granted to domestically produced sugar for the period up to October 1934, while the excise duty was reimposed at the equivalent of the preferential customs duty on imports from within the

Empire The subsidy was on a diminishing scale, with a minimum price to the farmers for their beet Under the stimulus of this subsidy, the beet sugar industry recorded rapid progress, the acreage under beet cultivation rose from 22,400 acres in 1924 to 396,500 in 1934, and the output of sugar increased from 24,000 tons to 600,000 tons The number of factories increased from three to seventeen during this period The cost of this development to the Exchequer has been substantial, up to February 1934 the total assistance, including subsidy and revenue abatement, totalled £39½ millions This subsidy was continued until September 1935, and a committee was appointed to suggest the most suitable form of future action in relation to the industry, and enable thereby the Government "to frame a long-term policy" The subsidy was continued for a further period of one year, pending the Report of the Committee, at a reduced rate, but involved a direct cost of more than £4 million

The Majority of the Committee held that there was no case for the continuance of the assistance At best, the subsidy was haphazard, inequitable, and extravagant The advantages obtained were quite inadequate for the expenditure involved In the event of Government deciding to continue long-term assistance, they recommended that the state assistance should be coupled with drastic reorganisation and control in the interest of the community The Minority Report, however, supported the continuance of state assistance for a further period, and favoured the method of a special levy on sugar consumption, which was rejected by the Majority Report as unsound

The policy outlined by the Minority Report was rejected as unsound even by the British economists "From the standpoint of the community as a whole," says Mr Richardson,[1] "the Majority view was largely unanswerable and its recommendations well founded There is general agreement that the industry has no prospect of becoming self-supporting and of competing with cane-sugar on any-

[1] Vide British Economic Policy p 157

thing like equal terms. The industry is small and restricted to a small part of the country. On economic grounds the charge on public funds during recent years was indefensible, while non-economic reasons, such as safeguarding sugar supplies in time of war, were inadequate to justify the costs."

The British Government, however, set aside the recommendations of the Majority Report and continued the subsidy in a modified form. The rate of subsidy will be periodically varied in accordance with changes in world prices of sugar, beet, etc. In 1936, the cost of the subsidy was about £3 million.

Again, the British Government granted a beef subsidy at the rate of over £4½ million a year to help the domestic producers. The shipping subsidy[1] is another important instance, and other instances can be multiplied.

Private export bounties have come into prominence with the growth of modern industrial combinations. These combinations make use of bounties with the intention of regulating competition between the different member-producers. Thus, the export bounties may be granted by the combination either to the members in the form of cash payments on the basis of quantity of goods exported, or to the non-member concerns using the products of the combination in the form of rebates.

The subsidies may be indirect. The indirect subsidies consist of the governmental measures introduced with the object of promoting the production or export of a commodity. Their forms are varied. The state may grant long-term loans or credits to the producers or exporters at low rates of interest or guarantee the loans or credits contracted by them with the banks. The Government export credit insurance schemes developed and perfected during recent years are instructive in this connection.[2] Exemptions

1. Vide, Zeis, P. M. American Shipping Policy; Dietrich, E. B. World Trade, Ch. VII.

2. Vide Dietrich, E. B. World Trade, Ch. VIII; The Problem of International Investment, Ch. VII.

may be granted from customs duties on imported machinery and materials used for establishing or developing a national industry Similarly, the national industries may be granted exemption from or reduction in fiscal duties on goods exported by them Third, the capital invested in new industrial enterprises may be guaranteed Fourth, some industries may be given the advantage of reduced transport charges in respect of raw materials used by them and their exports Fifth, national industries may be granted preference as regards the supplies to Government departments Sixth, the state may aid in price fixing and *stabilisation*

The fostering of production and export by subsidies, both direct and indirect, has become too common during the post-war period, with the result that the countries adversely affected by the imports of these subsidised goods have been led to adopt counter measures to protect their trade and industries These measures have at times been taken independently by the countries affected But often States have made mutual arrangements to exclude subsidies and these provisions have been incorporated in the commercial treaties negotiated by them

(6) Milling and Mixing Regulations—The milling and mixing requirements constitute an important part of the technique of modern commercial policy They regulate imports effectively Under these regulations, certain industries are required by law to use specified proportions of domestically produced raw materials For instance, Germany introduced compulsory milling regulations in July 1929, which prescribed the proportion of German wheat to be consumed by the German mills at 40 per cent The customs duty on foreign wheat was 65 marks per ton In August 1931 the proportion of German wheat was increased to 97 per cent and the duty on foreign wheat was raised to 250 marks per ton The effect of these measures was the practical exclusion of all imports of wheat and rye[1] In December 1929, France also introduced

[1] Vide, Trade Barriers, pp 380 81

compulsory milling regulation for French wheat, the quota fluctuating between 70 per cent and 97 per cent[1] Italy introduced compulsory milling regulation for wheat in June 1931 and fixed the quota at 95 per cent Belgium followed suit in 1932 on moderate lines, her quota varying from 5 to 25 per cent

(7) *Import Licenses.*—Under the licensing system imports of a particular commodity are not permitted unless licenses authorising such importation had been issued in advance The Government, therefore, can control the imports very effectively and promptly The issue of licenses can be discontinued at any time The undesirable imports can be excluded effectively without levying customs duties The system of licenses has invariably followed the introduction of the quota system France introduced the license system for the importation of meat, butter, livestock, cheese and sugar in 1931, which were subject to quotas Since 1932, Switzerland has introduced licensing regulations for nearly all agrarian imports The Belgian milling regulations of 1932 were followed by import licenses Czechoslovakia had an elaborate import license system for corn trade since 1926 The scope of the system was further extended in 1930, so as to cover the imports of cereals, meat and dairy products In 1931 the industrial goods were also subjected to import licenses Thus, the customs duties as an instrument for regulating the undesirable imports, have been relegated to the background, because they failed to secure the full measure of protection required

(8) Embargoes—Some countries, not being satisfied with the efficiency of other instruments of commercial policy have resorted to complete embargoes This is the most drastic instrument of commercial policy, and hence in practice complete embargoes are not very frequent For instance, Poland, not being satisfied with very high agrarian tariff, quotas, and linses, embarked

[1] Vide, Trade Barriers, pp 371-2.

upon a still more drastic policy in 1932 by a temporary but a total prohibition of all imports of some important agrarian products, such as corn, flour, hops, vegetables, fats, fruits, etc[1] Similarly, Bulgaria raised the duty on imports of raw sugar to 350 per cent in 1931, and imposed complete prohibition on imports so long as the home production remained unconsumed[2] Thus, it is clear that even the duty of 350 per cent could not keep out imports, and the embargo had to be imposed Hungary introduced import prohibitions in 1931

(9) **Monopolies**—Monopolies represent another powerful instrument of controlling the volume of imports Under these arrangements governmental agencies or specially designated private agencies are authorised to be the sole purchasers of imported commodities, although they may or may not be the sole domestic distributors of such commodities It is significant to note that this device for regulating imports has become very common since the depression For instance, in 1932, Czechoslovakia placed the whole of the grain and flour trade under the jurisdiction of a Czech importing syndicate Sweden established a sugar monopoly in 1931, which was designed to stimulate Swedish beet cultivation and sugar production Yugoslavia placed the imports and exports of wheat under state monopoly in 1930, and in 1931 brought the total imports and exports of grain within its purview

(10) **Sanitary and Administrative Regulations**—These regulations are in practice frequently operated in such a way as to provide an effective bar to imports In the commercial treaties we often find sanitary clauses, intended to protect the citizens from the contagion of undesirable articles If worked in proper lines these regulations would help the growth of trade and commerce between nations Unfortunately, these regulations have been frequently used to check the imports

1 Vide Trade Barriers, p 457

2 Vide Trade Barriers p 326

Joseph Grunzel has rightly pointed out that these prohibitions on importation (Veterinary Laws) were put in force in the particular period of low prices and were directed rather against competing regions than against infested regions For instance, Section 306A of the Hawley-Smoot Tariff Act prescribed an absolute sanitary embargo against any country as a whole when hoof and mouth disease or exposure to it is found to exist in any part of such a country As Secretary Hull pointed out, the real purpose of this regulation was "to establish what amounted to an embargo tariff under the guise of sanitary regulation" Similarly, the British ' Raw Apple Order of June, 1930" prohibited the importation of American apples between July 7th and November 15th except the two highest grades because of apple fruit flies discovered in shipment Apples from Canada were excluded from these regulations In 1924, New Zealand placed embargoes on grains, hay, livestock, plants, fruits and vegetables because of outbreak of hoof and mouth disease in California The United Kingdom followed the lead in 1931 Italy placed an absolute embargo on fresh fruits from the United States and certain other countries The World Economic Conference had therefore made the following recommendation in 1929 "International agreements which establish sanitary supervision, if they provide the contracting countries with adequate guarantees, should, without infringing sovereign rights, remove from the regulations any suspicion of disguised protection and should add to the stability of trade relations, which is one of the conditions of successful production" Unfortunately, this valuable suggestion was not adhered to by the advanced countries with the result that sanitary regulations restricting the flow of international trade have multiplied

Similarly, administrative regulations, which ought to facilitate the movement of trade, are being used to obstruct such a flow They are being used to help the growth of domestic trade and industries, to the detriment of international trade The raising of consular import and other administrative fees, the increasing severity of legislation

requiring marks of origin,[1] etc, have all restricted imports substantially The result is that trade becomes uncertain and variable

(11) **Imperial Preference.**—It has already been noted that a series of agreements were negotiated at Ottawa in 1932 between the constituent members of the British Empire These agreements conceded the principle of mutual negotiation on tariff policy within the Empire Concessions were made with the object of stimulating inter-imperial trade, and barriers against foreign countries were raised Other countries, having an Empire, have also entered into preferential commercial agreements[2] These agreements have led to artificial diversion and restriction of trade They have also created political rivalry between countries for extending imperial possessions As we shall point out later, the policy of Imperial Preference is essentially short-sighted and is largely responsible for the present economic and political complications

(12) **Exclusive Bilateral Commercial Treaties.**—Since the depression there has grown up a strong tendency for trade negotiations to take the form of bilateral, as opposed to multilateral, agreements The tendency towards the bilateralism of trade has not been confined to the restrictionist group, though it has arisen from that group The essential basis of bilateralism is the necessity of self-protection in the face of shrinking trade Where supplies of free exchange are limited, there is a natural desire to economise them as far as possible by so arranging the trade as to minimise the use of foreign exchange The increase of rigid bilateralism has, however, restricted the total volume of trade, as it takes place at the expense of multilateral transactions[3]

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1 While designed primarily to inform the purchaser with regard to the goods i e buyer the requirement of a mark of origin may used to serve protective ends. If it is difficult to affix a mark on a designed commodity or if the type of mark specified is unsuited to the size or shape of the commodity or if the commodity is highly specialised in type unsuiting it for other markets the expenses involved may be disproportionate Vide Dietrich E. B World Trade pp 99 100

2 Vide Barnes, L The Future of Colonies Sir Norman Angel Raw Materials Population Pressure and War Clark G A Place in the Sun, Raw Materials and Colonies The Problem of International Investments

3 Vide World Economic Survey 1935-36

These bilateral agreements are highly particularised in character and contain numerous trade arrangements such as customs quotas, tariff quotas, direct barter arrangements and the like Their duration is short, and they have been constantly revised The negotiation of these agreements has been guided very largely by the attempt of each country to insist that every other country shall buy directly as much from it as it purchases from the other country Often they are accompanied by clearing arrangements, under which the funds arising from the sales of goods between the pair of contracting countries are deposited in special clearing accounts and used only for payments between the two countries Such isolation of funds can be insisted upon by the country that had offered a better market to the contracting party in the past

Modern German commercial policy presents all phases of bilateral balancing of trade to an extreme degree, both in form and method of employment Germany has resorted to substantive bilateralism to find special markets for her manufactures in exchange for the raw materials and foodstuffs which she may require from time to time At the same time, she has vigorously pushed ahead with her policy of autarky and huge armaments The whole economic system is directed towards economic self-sufficiency and political hegemony As a result of this determined and rigid bilateralism the former natural channels of trade between Germany and the outside world have been considerably deflected

In short, bilateral trade is artificial, arbitary, and against the larger economic interests of the community It is an irregular trade, moving in an atmosphere of exclusive, reluctant, and half hearted concessions Special claims and special advantages are the bases of this trade Expediency, rather than efficiency, seems to be the acid test of modern commercial policy The pursuit of this policy may enable the states concerned to escape temporarily the unpalatable realities of internal economic problems and thus aid the realisation of the immediate aims of politi-

cians and dictators But it would be at the cost of material well-being of the people, economic stagnation must set in

(13) Restrictions on the Most-Favoured-Nation Clause —

The M F-N Clause which was originally intended to prevent commercial discrimination, cannot very effectively do so at present This is obviously due to the spread of quantitative regulations of trade by quotas exchange control and import license system adverted to above They spell discrimination Yet the M F N Clause cannot regulate them This obvious anomaly is due to restricted interpretation of the Clause The defect is not inherent in the Clause Proper interpretation of the Clause would remove this discrimination Some of the recognised legal exceptions to the M F N obligations are also responsible for the commercial discrimination For instance, Imperial Preference ought not to be recognised as an exception, it is dangerous It is a surprise how the system could sustain so long This type of exceptions tend to perpetuate the commercial discrimination which the M F N Clause is intended to remove The Imperial economic blocks which the exceptions to the M F N Clause have legalised are replete with discrimination and are important sources of economic and political insanity characteristic of the modern world

From the foregoing analysis it is obvious that the technique of modern commercial policy is replete with discrimination, the channels of world trade have been distorted and the flow thereof restricted The technique of modern commercial policy has become extremely complicated The economic implications of this new technique should, therefore, be very carefully studied and suitable remedies found In the following chapters attempts will be made to analyse the implications of some of these methods and suggestions offered, in the light of the study, for the future course to be followed

The conclusions of this chapter may be summarised as follows —

(1) The Great War created new economic problems which required a great deal of foresight and mutual understanding between nations for right solution The Treaty of Versailles shows a conspicuous lack of foresight The terms of the Treaty further complicated the difficult situation

(2) Economic policies pursued by the creditor countries during the post-war period failed to provide sound foundations on which the world economic system could be rebuilt Half-hearted and faulty economic policies pursued by the more important countries made the crash, that subsequently followed, inevitable

(3) The trade depression and the economic and political uncertainty is responsible for the development of new technique of commercial policy which has restricted international trade, reduced the income of the people and led to colossal unemployment, which manufacture of armaments is trying to conceal Material well-being has suffered considerably

(4) It is imperative, therefore, that the dangerous implications of this commercial policy should be examined and the international economic relations improved

CHAPTER III

COMMERCIAL TREATIES AND TARIFF BARGAINING METHODS

In the preceding two chapters we have traced the evolution of modern commercial policy and analysed, in brief, the recent developments in the technique of protectionism This historical analysis provides us with a background for the detailed study of the nature, form, contents and the working of modern commercial treaties In the present chapter we shall study in detail the bargaining methods, because the form of commercial treaties varies a great deal with the bargaining methods employed It is essential to note that discrimination has played an important part in the evolution of modern economic policy[1] Sometimes the commercial treaties themselves have been used to obtain exclusive concessions, which has further complicated the nature of discrimination, instead of removing it, and modified the structure of commercial treaties Exclusive bilateral commercial treaties are an instance In fact, the technique of protectionism evolved since the depression has profoundly modified the structure of commercial treaties and the bargaining methods employed in negotiating them In addition to the tariffs, which have been raised to an unprecedented level, the bargaining methods have been further complicated by quotas extensive use of exclusive imperial preference, exchange control, clearing agreements, subsidies, etc The negotiation of commercial treaties has, under the new methods of bargaining, become a very difficult task, it has become more of an art In the following pages, therefore, we shall study the nature, contents, objects, and forms of commercial treaties and the bargaining tariffs used in negotiating them

1 The tariff policies and bargaining tariffs of the Continental European nations for several decades have included formal provisions for discrimination While the tariff system has strongly tended to work itself out in practice to equal treatment of the commerce of all nations it has been built on the assumption that discrimination and inequality are natural features of commercial policy and are to be removed only by mutual agreements among sovereign states. Vide Page W T European Bargaining Tariffs, p 3

The Nature of Commercial Treaty.—A commercial treaty may be defined as a contract regulating the commercial relations between the parties[1] It is essentially bilateral, though the benefits are not always reciprocal For instance, the *Anglo-Japanese Commercial Treaty* of 14th October, 1854, is non-reciprocal, for Article V provides "In the ports of Japan either now open or which may hereafter be opened to the ships or subjects of any foreign nation, British ships and subjects shall be entitled to admission and to the enjoyment of an equality of advantages with those of the M F Nation, always excepting the advantages accruing to the Dutch and Chinese from the existing relations with Japan"[2] Similarly, the *Anglo-Greek Treaty* of 19th December, 1886, provides for the non-reciprocal advantages in favour of Britain Article IX of the Treaty lays down "The contracting parties agree that in all matters relating to commerce and navigation, any privilege, favour, immunity whatever which either contracting party has actually granted or may hereafter grant to the subjects or citizens of any other state shall be extended immediately and unconditionally to the subjects or citizens of the other contracting party, it being their intention that the trade and navigation of each country shall be placed in all respects by the other on the footing of the most-favoured-nation"[3] Instances can be multiplied Such non-reciprocal treaties are usually entered into between parties one of which is strong and the other weak The Peace Treaty entered into with Germany, after the Great War, contains similar provisions

The contracting parties are usually nations, two or more The contracts are entered into by the authorised agents of the States concerned It is not necessary that the contracting parties must always be independent sovereign states For instance, the Indo-British Trade Agreement, signed at Ottawa, was entered into between the British

1 Dr Gregory defines a commercial treaty as "an instrument regulating for a period of time (which may be fixed by the instrument or may be indefinite as depending on the will of the parties themselves), the commercial relations between two or more states Vide Tariffs, p 441

2 Ibid p 435

3. Ibid, p 434

Government and the Government of India India is not a sovereign state These agreements are entered into by the executive authorities of the states concerned

Sometimes, the Legislature prescribes the scope within which the Executive can negotiate, and the treaties thus negotiated, if within the ambit, do not require subsequent ratification of the legislature If they go beyond the limit laid down by the legislature, they are *void ab initio*, and the formal declaration to that effect may be given by the judiciary Such is the case with the United States of America, where the President is empowered to negotiate commercial treaties within the limits laid down by the Legislature The Act to amend the Tariff Act of 1930 (known as the Trade Agreements Act) approved on June 12, 1934, authorises the President of the United States to enter into reciprocal agreements with foreign governments "for the purpose of expanding foreign markets for the products of the United States" But in negotiating such agreements the American duties on goods covered by the agreement "shall in no case be increased or decreased by more than 50 per cent" The most important feature of the new Act, however is the absence of any requirement of Senate or Congressional approval of trade agreements entered into under the Act This facilitates the negotiation of treaties It is very difficult for a reciprocal trade policy to succeed where agreements are in every case subject to legislative ratification [1]

In certain democratic countries there are no restrictions imposed upon the discretion of the Executive in according advantages, concessions or privileges while negotiating a commercial treaty, but the treaty, before it can be enforced, must be approved by the legislature Such is the British practice The consent of the Parliament is not difficult to obtain, because the Executive represents the party with a majority in the legislature Again, in this case the Executive does not find its authority fettered

1 Past American experience proves this beyond reasonable doubt Vide Dr H J Tasca. The Reciprocal Trade Policy of the United States pp 43-44

while negotiating a treaty, nor can the nature and scope of the concessions be gauged beforehand This practice, therefore, is best suited to the British character and constitution British economic history has shown remarkable efficiency of this device in commercial bargaining

In a country like India the commercial treaties with foreign countries are negotiated largely by the Government of India in consultation with the British Board of Trade The Government of India may also seek the advice of non official advisers, who are nominated by the Government and not elected by the legislature But the Government of India is not bound to follow the advice tendered by these advisers Thus, the Government of India in consultation with the British Board of Trade may enter into any commercial treaty without even consulting the representatives of the Indian people, there is no statutory obligation to do so Even after the treaty has been formally signed by the British Minister, or his authorised agent, on behalf of British India, the Government of India is not bound to consult the Indian legislature before putting it into force Nay, even if it is definitely rejected by the legislature, it may be put in force, as has been the case with the Trade Agreement between Great Britain and India of March 1939

The Contents of Modern Commercial Treaties.—Modern commercial treaties cover a wide range of subjects [1] They may relate to admission of diplomatic and consular officers, their rights and activities, the establishment of foreign firms and the status of foreign travellers, legal and police protection to foreigners, means of communication and transportation, navigation, quarantine and harbour regulations and dues relating thereto, conditions for importation, exportation, transit, transfer and warehousing of merchandise, tariff and customs laws, bounties and drawbacks, internal duties and local dues, coasting trade, and port to port trade with foreign cargoes, the protection of patents, trade marks, copyrights and other industrial

1 For details see W S. Culbertson "Encyclopedia of Social Sciences," Vol. IV p.2 .

property rights, etc. Apart from certain miscellaneous provisions, the contents of a modern commercial treaty may be conveniently grouped under four heads [1] (a) consular matters, (b) trade and foreigners, (c) transport questions, and (d) trade and tariff questions

With the rapid growth in the means of communication, closer interdependence of nations, production for foreign markets, integration of industry, increased specialisation in production and international divison of labour, marked expansion in modern commerce, the commercial intercourse between nations has increased considerably and has led to the emergence of, what is popularly known as, tariff treaty [2] In other words, the tariff and trade questions have increased so much in importance that they have become subject matters of separate treaties, quite apart from other subjects This is not all To-day the tariff questions have become so prominent that the tariff agreements have come to be known as commercial treaties In the present study we propose to use the term in this restricted sense, unless otherwise stated, because our primary concern is to study only those treaties which regulate the import and export of goods

The Objects of Commercial Treaties—The next important question that arises is to note the objects with which commercial treaties are entered into In practice, the objects are varied, but the more important of them may be grouped together under two broad categories (1) to obtain an equality of trade conditions with other countries, or (2) obtain a preferential treatment over other states The first objective is essentially one of eliminating discrimination in commercial practice The discrimination may take two forms, the importing state may discriminate between the different foreign importers by according to some of them better advantages, concessions or privileges

1 Vide, Prof G Haberler "Theory of International Trade" p 360

2 It is very difficult to draw a clear cut distinction between the commercial treaties in general and the tariff treaties because the former is a genus and the latter a specie As Dr Gregory says "No rigid line of distinction can be drawn between the genus and the species but to the other technical terms of 'Treaties of commerce and Navigation' or 'Friendship Commerce and Navigation' there must now be added 'Treaty of Commerce Customs and Navigation'" Vide, Tariffs p 441

than those accorded to others, or it may treat all the importers on the same footing but extend to the domestic producers more privileges than those accorded to foreign countries The protection against the first form of discrimination is provided by the inclusion of the "most-favoured-nation treatment" The second form of discrimination is eliminated by including the "parity clause" which provides that the treatment given by a state to the citizens and goods of the state with which the treaty is made must not be worse than that given to its own citizens The guarantee thus provided by the "parity clause" is known as "national treatment"

The term "*national treatment*" is not found in commercial treaties, but the principle is incorporated in involved legal language The phrase "national treatment" is therefore less familiar than the "most favoured-nation treatment," though both the pledges are common in commercial treaties The national treatment, like the most-favoured nation treatment, may or may not be reciprocal It may be limited in its scope The nature, scope and extent of the treatment pledged in any treaty must be determined in each case by the language employed[1] The usual form in which the pledge for reciprocal national treatment is provided in commercial treaties can be seen from the treaty of 1815 between the United States and Great Britain, which lays down "No higher or other duties or charges shall be imposed in any of the ports of the United States on British vessels than those payable in the same ports by vessels of the United States, nor in the ports of any of His Britannick Majesty's territories in Europe on the vessels of the United States than shall be payable in the same ports on British vessels"[2]

The pledge of national treatment is often restricted in its scope *In keeping with the growing national consciousness*, countries have generally tried to reserve for their own citizens certain rights and privileges which are not

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1 Vide W S Culbertson "International Economic Policies" p 20
2 Ibid pp 28-29

extended to the aliens For example, the United States has reserved the coasting trade exclusively for vessels of its own citizens Therefore, when the American commercial treaties contain the pledge of national treatment in sufficiently broad terms, there is invariably an express provision excepting the coastal shipping For instance, the Convention of Commerce and Navigation of 1852 between the United States and the Netherlands provides that neither party shall impose upon the vessels of the other, from whatever place arriving any duties or port charges of any kind or discrimination which shall not be imposed in the like cases on the national vessels Thus, the terms of the general guarantee are sufficiently wide The Convention, therefore, provides for an express exception to the effect that "The present arrangement does not extend to the coasting trade and fisheries of the two countries respectively, which are exclusively allowed to national vessels "[1] In short, the guarantee of national treatment is often subject to exceptions, which means discrimination between the domestic and foreign producers But it should be noted that the guarantee of national treatment is more valuable than that of the most-favoured-nation treatment, for the latter provides protection only against discrimination between foreign importers *inter se* In other words, the M F N treatment provides that all foreigners shall be treated alike The national treatment guarantees that the nationals and the aliens shall be treated alike In India national treatment is accorded to British trade

The Form of Commercial Treaties.—According to Dr T E Gregory the tariff treaties can assume the following forms [2]

(1) Most favoured nation treatment only

(2) (a) Grant of part of the minimum tariff only

(b) Grant of whole of the minimum tariff only

(c) Grant of whole of the minimum tariff and conventionalisation of

1 Ibid, p 37
2 Vide Tariffs p 447

tracting state has no claim In short, such a treaty leaves unrestricted scope for tariff discrimination and provides no assurance for the stability of tariffs

Where a commercial treaty grants the whole of the minimum tariff, without the most-favoured-nation pledge, the situation is not materially different from that in the preceding case, except that the contracting state can claim the future autonomous tariff reductions in the entire minimum tariff Tariff discrimination remains and is encouraged There is just a slight improvement in the situation

Sometimes a commercial treaty may accord the whole of the minimum tariff, without the most-favoured-nation pledge, and in addition contain a stipulation binding the grantor state not to increase the rates as laid down in the treaty for a specified period In this case the grantee state enjoys better advantages than in the preceding two cases The stability of tariffs is secured for the period agreed to But here, too, there is a scope for discrimination, for, due to the absence of the most-favoured-nation pledge, there is no obligation to extend to the grantee state the further reductions in rates that may be accorded in future to other states

A country may sometimes grant, as a result of diplomatic bargaining some special concessions in the general tariff by way of convention in a commercial treaty, without the most favoured-nation treatment Here, the concessions are accorded for a definite period specified in the treaty The grantee can neither claim the concessions accorded to other countries, at the date of the treaty, in respect of the articles not specified therein, nor any of the future reductions that may be made even on the articles included in the treaty The scope for discrimination, therefore, remains, though tariff stability is achieved

It is also possible that a country may accord, as a result of commercial bargaining, special concessions to the contracting state and at the same time grant all other con-

ventionalised rates as well, without the most-favoured-nation treatment Such a commercial treaty extends the conventional tariff in full to the other contracting party, for a definite period But due to the absence of the M F N Clause in the treaty, the contracting party cannot claim as a matter of right the concessions that may be granted at a future date to third states Discrimination, therefore, remains

The other, and more important forms of commercial treaties are where the Most-Favoured-Nation Clause is combined with the tariff concessions The possible forms of the *M F N Clause are* eight [1] (1) conditional, reciprocal and limited, (2) conditional, reciprocal and unlimited, (3) conditional, non-reciprocal and limited, (4) conditional, non-reciprocal, and unlimited, (5) unconditioanl, reciprocal and limited, (6) unconditional non-reciprocal, and limited, (7) unconditional, reciprocal and unlimited, (8) unconditional non-reciprocal and unlimited The M F N Clause has played an important part in the development of modern commercial policy and has moulded the form of commercial bargaining considerably We shall study in detail in subsequent pages the efficiency of the different bargaining methods when the most-favoured-nation pledge is coupled with tariff concessions For the present it is sufficient to note that the forms of commercial treaties differ according to the form of the *M F N* pledge and the tariff concessions accorded

Tariffs: Their Purpose—We shall now proceed to analyse the tariff systems and their place in modern commercial policy Tariffs, notwithstanding the new developments in the technique of commercial policy since the depression, continue to play an important part in determining the flow of international trade [2] They form an important instrument of commercial bargaining Therefore, an analysis of

1 For further details see Dr T E. Gregory: Tariffs, pp 450-55 "Reciprocity and Commercial Treaties pp 443-50

2. Mr Fetter has rightly remarked, "The tariff is important as a public issue today, not as a problem in the raising of revenue but as a problem in the use of the power of the state to direct economic life. Vide Fetter F W: The New Deal and the Tariff Policy, p 3

the tariff systems is invaluable for a proper study of the technique of modern commercial policy

Tariffs for Revenue—(1) Sometimes the tariff duties are imposed on the goods imported from abroad with the object of securing revenue Here foreign trade is used as a source of taxation Since the primary purpose is to secure revenue to meet public expenditure the tariffs are so framed as not to check the flow of international trade, due account is taken both of the nature of demand and the conditions of supply If the tax is imposed on imports which are also produced by domestic industries, they are invariably supplemented by a similar tax on domestic production in form of an excise duty, to equalise the conditions of competition and secure adequate revenue Revenue duties play a very important part in modern public finance The amount of import duty varies according to the nature of the commodity and in proportion either to its value (*ad valorem* duties) or to weight or quality (specific duties) *The ad valorem duty is based essentially* upon the value of the article imported, it is a fixed percentage of the value per physical unit The specific duty is a fixed sum of money charged upon each unit of quantity imported The question of valuation in this case does not arise

The Specific Duties—In practice, one finds the specific duties more common, they have largely displaced the *ad valorem* duties The specific duties are more convenient to administer This is so because the physical and chemical properties of a commodity can be more easily determined than its value,[1] though with the recent tendency towards increased specialisation of tariffs the difficulties have increased considerably[2] But against these administrative advantages in favour of specific duties must be set certain disadvantages incidental to such a practice The specific duties are generally regressive in their incidence,

1 They depend less upon the decision of customs officials and are more automatic in their application The opportunities for evasion and corruption are minimised

2 Producers have tried to evade taxes by so fabricating an article that it avoids the classification intended for it

because the incidence of the tax on cheaper commodities becomes more heavy This is apt to rouse public criticism We may, therefore, consider tbe incidence of the duty with the purpose for which it is levied If the specific duty is imposed for revenue purposes it violates the well known maxim that taxation should be based upon the ability to pay and ought to be opposed Where, however, it is levied for protective purpose, the criticism loses much of its force The *ad valorem* duties, on the contrary if properly determined are more equitable since the duty can be adjusted to the value of of the commodity It may be noted that tariff specialisation can partly remove the regressive character of the specific duties But this measure will not go far enough Poor people will have to bear the brunt Further, the incidence of the specific duties varies inversely with the price level, which is undesirable In certain cases the specific duties are not applicable at all This is the case with the articles whose value does not depend upon physical attributes, *e g* paintings

The *Ad Valorem* Duties—The greatest defect of the *ad valorem* duties is that it is difficult to determine precisely the value of the articles to be taxed There are different kinds of prices We have the f o b price, the c i f price, the invoice price the price specially declared by the importer, the market price of the articles at the time when the contract of sale is executed the price of the goods at the time of crossing the frontier Which one of these prices should be the basis of taxation ? To avoid inconvenience, the values are officially fixed But it may be noted that a reliable valuation of the articles is both difficult and costly

2 **The Protectionist Tariff**—The tariff duties may be levied with the object of protecting national industries The evolution of modern tariff policy brings to relief the fact that the road to internationalism lies through healthy nationalism,[1] and therefore for a smooth working of the international economic mechanism it is essential that the

1 See the review of commercial policy in the first chapter

claims for reasonable national economic development should be recognised and respected The classical economists did not fully appreciate the value of this national sentiment and underestimated its potential strength Ricardo asserted that under a system of perfectly free commerce, each country naturally devotes its capital and labour to such employments as are most beneficial to each But, Fredrick List rightly denied that this sweeping inference was warranted by the reasoning upon which it was founded Of course, the classical analysis clearly showed that the direct and immediate effect of unimpeded foreign trade was to increase the national dividend But, the direct and immediate effects are not the sole effects The object should be to bring out a most efficient and effective utilisation of national resources "The power of producing wealth is infinitely more important than the wealth itself"[1] Consequently, "the nation must sacrifice and give up a measure of material prosperity in order to gain culture, skill, and power of united production, it must sacrifice some present advantage in order to ensure to itself future ones It is true that protective duties at first increase the price of manufactured goods, but it is just as true, and moreover acknowledged by the prevailing economical school, that in the course of time, by the nation being enabled to build up a completely developed manufacturing power of its own, those goods are produced more cheaply at home than the price at which they can be imported from foreign parts"[2] Thus, a reasonable and sagacious protectionist policy, though immediately it imposes a burden upon the consumers, provides in the long run considerable material and non-material advantages, the sacrifice is essentially temporary The ultimate gain is apt to be more than the immediate loss[3]

A country requires an industry not only as a means of directly satisfying its needs, but also as a machine which

1 Vide List F A National System of Political Economy p 133

2 Ibid, pp 144-45

3 In short a nation like an individual may be well advised at certain stages of its history to dispense with present wealth for the sake either of education or of insurance Vide Prof Pigou "Protection and Preferential Import Duties p 14

creates buying capacity to be utilised in purchasing foreign goods and services The ability to satisfy international buying capacity is an important consideration in assessing the national importance of an industry and its claim for protection The advantages derived from international exchange depend upon the efficiency of domestic production and the price paid for the goods imported from foreign countries M Manoilesco rightly argues that what imports cost to a country is the function of two variables, the quantity and cost of her own commodities she gives in exchange for them If a country produces two different kinds of goods with two different degrees of productivity, it is profitable to concentrate the application of labour and capital in the production of those commodities alone which have larger productivity The comparative superiority of each of the two kinds of goods in the foreign country is of no importance Goods with a large comparative advantage in relation to the foreign country should not be produced but the goods which under the conditions of home production have a greater absolute productivity should be produced It is upon the most absolute productive activities that national effort should be concerned [1] In short a reasonable protectionist policy can help a great deal in improving the technique of production in backward countries

3 **Tariff Duties are also used for Bargaining Purposes** — During recent years the use of tariffs for bargaining purpose has increased It is essential to note however, that the use of tariffs for commercial bargaining may involve a departure from the principle of equality of treatment The form of tariff varies with the object in view Multiple column tariffs are used to extend tariff concessions to imports from different countries in accordance with the amount of favourable treatment received from those countries Conventional rates are specified rates agreed to between the countries in their special bilateral treaties These rates may be either exclusive according to the terms

1 Vide M Manoilesco: "The Theory of Protection and International Trade" p 89

of commercial treaty or they may be generalised under most favoured nation treatment Penality tariffs are used only in case of reprisal Seasonal tariffs are used to accord more favourable treatment to goods imported during a particular season They are used primarily to permit the import of agricultural products during the season when domestic supplies run short Tariff quotas are used to permit a limited quantity of an imported article at a lower tariff Tariff quotas become an effective bargaining instrument when the quantity of imports permitted is small relative to the domestic consumption but large relative to the *export of the favoured country*

4 **Tariffs are used for According Exclusive Preferential Treatment to the Products of Certain Countries**—This is true of Imperial Economic Blocks Customs Unions Regional Groups based on ethnic historical or geographical ties All these tariff preferences are regarded legitimate exceptions to the most favoured nation treatment

5 Some countries have made use of **tariffs for bringing passive balance of trade into equilibrium** In this case multiple column tariff is used and higher rates are imposed on goods imported from countries with which there is an adverse balance of trade This device is used to effect bilateral balancing of trade

The Tariff Systems—The tariff systems can be conveniently grouped into three broad types (1) Single line Tariff (2) Double line Tariff and (3) Triple line Tariff

The Single line Tariff—This form of tariff is the simplest and generally autonomously determined It consists of a *single schedule* of duties applicable to all imports irrespective of the country of origin Thus the possibility of discrimination is entirely eliminated under this system As an instrument of bargaining therefore it is very weak *Countries with single line tariffs* have very little to offer by way of concession in negotiating commercial treaties It is extremely inelastic and cannot promptly be adjusted to suit the needs of indigenous trade and industries

This form of tariff is more useful to a country which finds it profitable to pursue a non-bargaining commercial policy Here tariff is not used as an instrument of bargaining and making concessions The country adopting this form of tariff may either refuse to negotiate *ab initio*, or generalise the concessions agreed to as a result of negotiation, with the result that the new rate is substituted for the old one and the tariff remains single-line The duties are fixed with a view solely to securing national requirements, and no matter what their height and subsequent changes, the other contracting party receives a guarantee that it will not be subjected to any disadvantage or discrimination

The Double-line Tariff.—This form of tariff contains two schedules, based on the principle of charging two rates on some or all articles Both the rates may be fixed by the State at the very start, or only one rate may be so fixed and the other rate may result from the negotiation of commercial treaties These second rates may not affect all the articles The general presumption is that the country which adopts this form of tariff has important commercial relations and believes in a policy of commercial bargaining With its growing home industries and trade it feels the necessity of establishing new commercial contacts and cementing the old ones by negotiating commercial treaties and offering tariff concessions There are two main types of this tariff

(1) **The General and Conventional.**—It should be noted that the general and conventional tariff, properly so-called, is quite distinct from the single-line tariff having conventional elements in it, for the conventional duties arrived at by negotiation may be generalised by the M F. N Clause and substituted in place of the general rates The result is that the single schedule which such a system would contain embodies both the autonomous and conventional elements. With the success of the policy of commercial treaties the conventional element of the tariff increases. Thus, such a tariff is no longer a bilateral or

a double-line tariff It is essentially a single-line tariff with a conventional element in it

The general and conventional tariff must be bilateral, having two schedules, one fixed by the legislature and the other resulting from the concessions obtained from foreign countries through commercial treaties on the basis of reciprocity In this case, therefore the tariff as it leaves the hands of the legislator is an autonomous, a single-line tariff, and complete freedom is accorded to those in charge of negotiating commercial treaties and making concessions Thus, the autonomous tariff, with its general rates applicable to all countries, forms the basis of negotiation and treaties are entered into with individual foreign countries and concessions in the general rate accorded The aim of a country pursuing such a policy is to negotiate commercial treaties with almost all important countries The concession rates, contained in the different treaties, constitute the conventional tariff These rates may be extended to other countries by the operation of M F N Clause in the commercial treaties [1] In this connection it is essential to note that the general tariff, autonomously determined, continues to apply to the goods imported from the countries with which treaties have been negotiated to those articles on which concessions have not been offered Thus, we have two schedules, one the general and the other conventional The most valuable result of such arrangements is the relative stability of tariff duties,[2] it helps the growth of industry and commerce The consolidation of tariff duties in commercial treaties imparts much needed confidence to the business community and

enables them to plan ahead their schemes of industrial development

This form of tariff originated in Germany in 1891 as an important instrument of commercial bargaining Till that time Germany followed the tariff policy outlined by Bismarck in 1879, which was based on the single-line autonomous tariff The period between 1879 and 1891 was of immense importance to Germany because it was during this interval that German industries, protected under a strong tariff wall against foreign competition, could consolidate and strengthen their position It was an era of *remarkable German industrial development*,[1] which enabled Germany to become one of the foremost industrial nations of the world No wonder, therefore, that as a result of this expansion, the German industries sought an entry into foreign markets But, by now the other European countries had also adopted the protectionist policy with a view to fostering their own industries Germany, therefore, had to resort to tariff bargaining as the only effective instrument for reducing the tariff barriers in foreign countries against her goods She started these commercial negotiations with other countries, having the single-line autonomous tariff of 1879 as the general tariff, and conceded tariff concessions on the basis of strict reciprocity to the countries offering suitable reductions in their tariffs The new rates agreed to in the commercial treaties constituted the "unconventional" schedule The treaties thus concluded were renewed in 1903, to remain in force till 1917 Under this policy the German goods could capture markets they would otherwise have found very difficult to do Similar tariff bargaining policy was followed by Italy, Austria, Switzerland, Spain, Russia, etc In short, it would not be an exaggeration to say that the "general and conventional" principle dominated the tariff policy of Europe before the outbreak of the Great War.

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1 "Whilst the burden of taxation on imports is heavily felt by the masses of the people and by many industries the protection afforded by the tariffs has encouraged the steady growth of manufactures which before 1879 were in their infancy, and the introduction of many which were then unknown" Vide Higginson, p. 11

From the foregoing brief review it will be seen that the great merit of this form of tariff is that it tends to promote tariff stability Through the commercial treaties, and the mutual tariff concessions agreed to therein, the conventional rates are substituted in place of the general rates and they are definitely fixed for fairly long periods, usually ten or twelve years [1] Under the extensive network of commercial treaties containing the M F N Clause the system assures the countries concerned that there will be no general tariff upheaval during the period of the life of the treaties Further, it becomes more convenient to improve the structure of industries and plan for future expansion

The general and conventional tariff system, however, has its defects It requires a protracted bargaining process before the final concessions can be mutually agreed upon In the meantime, the general tariff, usually higher than that warranted by the domestic economic requirements, is enforced which penalises both the domestic consumers and the foreign producers In this process of hard bargaining even a slight hitch may break the negotiations and make the general tariff permanent Further, it is necessary that before the existing commercial treaties expire, the new treaties must finally be agreed upon lest it should lead to sudden and violent tariff changes

It is interesting to note that where the treaty making power is in the hands of the Executive, the general and conventional tariff system tends to diminish the relative importance of the legislative authority and tariff negotiation and administration fall mainly into the hands of officials This was one of the reasons which induced the United States to abandon her single-line tariff in 1909 and adopt the "maximum and minimum" system

(2) **The "Maximum and Minimum" Tariff**—This is the other form which a double-line tariff may take This form of tariff contains two sets of rates, both being autonomously determined The country adopting this practice

feels the necessity of making tariff concessions, and yet does not find it desirable to give to those entrusted with the task of negotiation a perfectly free hand, as is the case under the general and conventional system Therefore, the legislature fixes both the sets of rates, and the negotiators can never offer concessions greater than those provided in the minimum schedule No doubt, even in this case the diplomats offer the minimum rates to other countries strictly on the basis of reciprocity, but the discretion of the Executive is considerably circumscribed

The maximum and minimum tariff takes two forms in practice In the first form two sets of rates are fixed by the legislature and incorporated in two schedules The schedule containing higher rates is to be used for bargaining purposes, whereas the lower schedule represents the minimum economic requirements of the enacting country from which no concessions can be ordinarily obtained The minimum schedule shows the definite and fixed lowest limit to which concessions can be accorded by the executive at any time Beyond that the executive has no authority, it must ask for it from the legislature. In such a case, therefore, the executive may accord the minimum tariff in whole or in the part to the foreign country with which a commercial treaty has been negotiated But, it should be noted that full minimum rates have to be conceded to the contracting party The executive either accords the minimum rates, or refuses concession in toto, there is no intermediate stage Thus, the nature and scope of the concessions, which a country adopting this form of tariffs can accord, are known to the other contracting party In the pre-war period, France was the leading exponent of this type of bargaining tariff She conceded to the other contracting party in her commercial treaties some, or all, of the minimum tariff rates The concessions were generalised through the M F N Clause of her commercial treaties, with the result that the French minimum tariff was extended to almost all important countries[1]

1 For fuller details see Chapter I

maximum and minimum rates, and the preferential rates intermediate between these two rates, are applicable to the goods of the mother country or the colonies These preferential rates are the result of the policy of imperial preference, an attempt to grant exceptional treatment to a particular source of supply The intermediate rates are employed as an instrument of negotiation for securing preferable tariff treatment to home products in foreign countries, and these rates may be extended to any foreign country on the basis of commercial reciprocity It may be noted that when the intermediate rate arises out of the maximum and minimum tariff system, it may be based on the existing minimum, and in that event it will usually be lower than the minimum, or, it may be based on the existing maximum, when it will usually be intermediate between the other two rates. Similarly, where the intermediate rate grows out of the general and conventional tariff system, it may be based either on the general or the conventional rate

Relative Utility of the Tariff Systems.—From the standpoint of the domestic industry and commerce the autonomous tariff, whether of the single or double-line type, is preferable to any other, because the legislature has full freedom to provide for the necessary tariff security Due to the absence of conventionally bound rates, tariff duties can be promptly adjusted to suit the national economic requirements. No wonder, therefore, that under the autonomous system the tariff changes are usually gradual, which secures tariff stability Under the conventional system, on the other hand, based on a net work of commercial treaties, the tariff changes are rather violent, as the termination of treaties forces a revision of the entire tariff system. Besides, to effect suitable alterations in tariff rates, based on a conventional system, a large number of commercial treaties have to be negotiated anew The process of negotiating commercial treaties is extremely complicated, difficult and spread over time A number of vested interests grow up during the tenure of the treaties

with the result that the reconciliation of their claims becomes an unenviable task Commercial negotiations are as a rule protracted This interval, usually long is marked by uncertainty which paralyses trade and industries For the triple-line tariff it may be said that the element of imperial preference causes considerable international friction and is the root cause of the policy of autarky in vogue since the inception of the depression Besides it increases the difficulties of those in charge of negotiating commercial treaties the adjustment of conflicting interests becomes a very delicate and difficult task To this must be added the administrative difficulties

Purpose of Bargaining Systems —

Equality of Treatment—Having reviewed in broad outline the more important tariff systems we may now examine the objectives of commercial bargaining The objectives are determined by the economic conditions of the country resorting to it particularly the stage of its industrial development The equality of treatment is one of the most important objectives of tariff bargaining or negotiation of commercial treaties Every country desires that its exports in foreign markets shall not be subjected to an unfair treatment so as to impair its competitive capacity as against other foreign competitors In other words the primary need of every country is to secure the advantages in export markets equal to those accorded to other competitors This purpose is achieved by utilising the tariff as a retaliatory or penalty measure to remove or to forestall discrimination

Commercial Equality in the Negative Form—This equality of treatment assumes a negative form under which the contracting parties undertake that in no case should the ' products of one contracting party be subject when imported into the territory of the other to a less favourble treatment than that granted to the like or similar com modities of any third party ' This attitude was adopted by those countries which wanted to keep their tariff autonomy unimpaired Under this system the height of

tariffs is regarded as purely a domestic affair of the country imposing them, to be determined by the requirements of internal trade and industries, with which foreign countries having treaty relations have no right to interfere Besides, there is no assurance in the commercial treaties thus entered into as regards the continuity of particular tariff levels, which leads to tariff instability This is so because the contracting parties, while providing for commercial equality retain full liberty of changing their tariffs as and when they deem it necessary to suit the national requirements The country adopting such an autonomous tariff, can by merely assuring commercial equality to the contracting parties, avail itself in full of the advantages accorded by other countries, and at the same time keep its own tariff entirely independent of any treaty obligations

As an instrument of commercial bargaining the autonomous tariff, which assures commercial equality in this negative form, is very effective in so far as it enables the country resorting to it to sit on the fence and reap the benefits accorded by other countries In the history of commercial policy cases are found where a country with an autonomous tariff, prohibitive in its height, has succeeded in getting from the other countries entering into treaty relationships liberal tariff treatment in return for prohibitive treatment This is so because the single-line tariff provides a guarantee against discrimination It is evident, therefore, that the single-line autonomous tariff, prohibitive in effect, may be used as an effective instrument for sharing the advantages accorded by the bargaining countries as a result of long haggling, merely because such a system affords adequate protection against discrimination

The negative assurance provided by the autonomous tariff, though useful in commercial bargaining, has its most obvious limitations In addition to the tariff instability, such a form of commercial bargaining creates international animosity and suspicion against the country adopting it, though foreign countries may continue to ac-

cord favourable treatment in return for commercial equality Therefore as a long term instrument of tariff bargaining this system is defective But as a temporary expedient, to assist the growth of rising domestic industries it is invaluable and very effective A protectionist country may profitably use this method of tariff bargaining

Equality of Treatment in the Positive Form—In view of its obvious defects the negative formula of commercial equality has been replaced by the positive guarantee both as regards the favours granted in the past as well as those to be granted in the future This is popularly known as the unconditional and unrestricted M F N Clause The stipulation provides that any favour or privilege which may hereafter be granted either in virtue of autonomous measures or in virtue of commercial conventions to the commodities of any third state whatever shall be extended to the like or similar commodities of the other contracting party It is essential to remember that the guarantee of M F N treatment has been one of the primary objectives of commercial treaties and tariff bargaining Under such commercial treaties the contracting parties can claim as a matter of right any privilege that may be granted to a third party This form of commercial treaties is more useful because it not only protects the contracting parties from discrimination but also provides for further improvement of commercial relations in future This prospect of future improvement lies in the M F N Clause contained in the treaties favours privileges and concessions granted to third parties have to be extended immediately and without compensation to the contracting party

In practice it has been found that the commercial treaties containing the M F N Clause provide only *de jure* reciprocity which has sometimes failed to guarantee *de facto* equitable treatment For instance the United States since 1922 though including the M F N Clause in her commercial treaties has scrupulously kept the height of her tariff independent of any treaty obligations She ensures to all countries equal rights and demands com-

mercial equality in return. There is no discrimination, but all are treated equally badly. *The greatest defect* of the *de jure* reciprocity[1] is that a country can follow almost prohibitive tariff policy so as to exclude the foreign commodities from her market and at the same time claim as a matter of right all privileges, immunities or concessions granted by other countries, which would facilitate the entry of her goods into foreign markets. That the M. F. N. Clause should not obstruct reasonable protection is admitted. But if it is so interpreted as to permit prohibitive tariff levels and tend to perpetuate them, international economic development would be seriously endangered. Such an interpretation of the M. F. N. Clause tends to neutralise the utility of the equality of treatment. This defect is not, however, inherent in the M. F. N. Clause, but is due to the faulty interpretation put upon it by the parties interested in driving a hard bargain, in keeping purely with the letter, rather than the spirit, of the Clause. Notwithstanding the aforesaid defect, in practice, of this form of commercial bargaining, the *de jure* reciprocity plays an important part in treaty-making.

Bargaining Tariffs to Stimulate Exports.—Another important objective of bargaining tariffs is to use import duties for stimulating exports. The tariff schedules are so constructed that through the process of bargaining, concessions may be exchanged for concessions. This is so because some countries have felt that the *de facto* reciprocity is more suited to their requirements than the *de jure* reciprocity. To achieve this *de facto* reciprocity the tariff systems, described above, have been variously used to extract the maximum gain out of the bargain. The conditional M. F. N. Clause has been used in commercial treaties to obtain *de facto* reciprocity. Under this system of bargaining each contracting party undertakes to extend unconditionally to

1 It must be conceded that there is great deal to be said for the principle of neither seeking nor granting any special advantage. If tariffs are regarded as unavoidable, then without doubt equality of treatment is beneficial in maintaining peace and good relations between states, for without such equality innumerable political causes of conflict would arise. It is of especial and vital importance for small countries that the world should keep at least in principle to this policy. Small countries would suffer heavily from the short-sighted policy of discriminating treatment. Vide Prof. G. Haberler, "Theory of International Trade," p. 373.

the other the privilege immunity or favour it may subsequently accord unconditionally to any third state, but those privileges which have been granted on specific conditions can be claimed only on the fulfilment of those conditions In practice, however, it is difficult to determine an identical or even an equivalent concession Therefore the tariff bargaining and the negotiation of commercial treaties under such a system presents very irksome problems and leads to waste of time and energy Besides, it leads to discrimination and increase in trade barriers This form of tariff bargaining, therefore, had a limited success, it failed to achieve the objective aimed[1] at

Attempts have been made to secure *de facto* reciprocity with an autonomous tariff, subject to conventional reduction of duties, through commercial treaties, on articles of special importance to the export trade of either of the contracting parties, containing the M F N Clause Under this system the autonomous tariff is gradually replaced by a conventional tariff, built up with concessions successively granted to countries with which treaties have been concluded This system however, has certain defects In the first place, it leads to tariff specialisation which causes discrimination It violates the spirit of the M F N Clause by discriminating against similar products of other countries In other words, under this form of the tariff the generalisation of concessions through the M F N Clause is shorn or its significance Further, it leads to padding of tariff rates to provide greater scope for commercial bargaining These padded rates are often enforced before starting negotiations, with the result that pending the negotiation of commercial treaties the prohibitive tariff distorts the channels of trade, and at times causes irreparable damage to commercial relations It leads to tariff wars In the pre-war period this defect was partly made up by the relatively long tenure of the treaties To-day this system leads to more frequent and violent upheavals

in tariff policy and obstructs the flow of international trade.

Sometimes the **Double-Line Tariff** with the M.F.N. Clause has been used to secure tariff reciprocity and at the same time maintain tariff autonomy. Here we have a moderate minimum tariff, determined strictly by the minimum requirements of domestic industries, which cannot be reduced. The general tariff, applicable to non-treaty countries, is essentially a fighting tariff. The difference between the two schedules is considerable, which is to be used for effecting equivalence between the advantages acquired and accorded. This system, however, is weak as a bargaining instrument and leads to tariff instability because minimum tariff is coupled with the M.F.N. Clause.

The Triple-Line Tariff system is used to make up for the shortcomings of the double-line tariff. The rigidity of the minimum tariff, which impairs its bargaining efficiency, is made up under this system which provides for the third schedule containing the conventional reductions of the minimum tariff. *The defect of tariff instability is also* removed, since the conventional rates can be consolidated through commercial treaties. The maximum schedule under this system becomes a fighting schedule. Thus, the triple-line tariff secures adequate protection to the domestic industry, preserves tariff autonomy in this respect, extends the M.F.N. treatment to other countries through commercial treaties, and, by effecting consolidation of tariff concessions, achieves tariff stability. But in its working the triple-line tariff system complicates the technique of commercial policy and adds to the difficulties of treaty negotiation.

Conclusions.—From the foregoing analysis of bargaining tariffs and the objectives they have been used to attain, it will be seen that when the measures were inspired by a liberal objective of obtaining concessions for mutual advantage they have had a marked success; but, where

tariff bargaining, with periodical revision and padding, was used merely to get an upper hand over the other contracting party it failed to achieve its proper objective and created chaos in commercial relations

The tariff bargaining conducted under the atmosphere of suspicion and distrust, with the intention of squeezing concessions from foreign countries, has been a failure It has rarely been successful in forcing another country to reduce its working tariff Both the parties to a treaty before starting commercial negotiations raise their tariffs to levels higher than those warranted by their reasonable economic requirements, to secure sufficient margin for bargaining, and the result is that often the rates agreed to in the treaty, as it emerges from the negotiations, are higher than those in force before the padding commenced The net result of tariff bargaining, conducted under an environment of mutual suspicion, is often an increase in tariff duties It is a poor device for stimulating international trade The improvement of trade, if it is to be lasting, must be mutual and be backed by a genuine and sincere desire on the part of both the contracting parties to remove their difficulties by perfect understanding, the analysis of the situation should be frank and unreserved It is well-known that no country can expect to increase its exports by means of a commercial treaty unless the other party is willing to increase its imports

To stimulate the growth of foreign trade, narrow commercial reciprocity should be given up As adverted to above, it makes the process of tariff bargaining complicated, irksome and wasteful It breeds discrimination The proper objective should, therefore, be equality of treatment in keeping with the legitimate national economic requirements The unconditional M F N Clause should form an integral part of commercial policy[1] and be granted with sufficient discrimination so as to compel the recalcitrant countries to give up their discri-

[1] See Prof J Viner The Improvement of Commercial Relations p 86 and Dr Leo Pasvolsky pp. 75-76

minatory practices Further the tariff classification should be simplified and the tendency towards increased specia lisation checked At the same time the tendency towards multiple tariff system should be definitely discouraged

Let us now briefly summarise the conclusions

(1) Tariff bargaining if conducted with a liberal out look and mutual understanding can substantially help to reduce the barriers on world trade Full and frank dis cussion will remove misunderstanding and improve inter-national commercial relations To achieve this objective tariff bargaining should be conducted with considerable tact On the other hand tariff bargaining conducted under an atmosphere surcharged with suspicion and ill feeling will raise the height of tariff barriers instead of lowering them[1] Tariff bargaining is essentially an art

(2) Equality of treatment should be the basis of tariff bargaining

(3) The unconditional M F N Clause should be an integral part of the policy of tariff bargaining

(4) Tariff classification should be simplified

(5) The tendency towards multiple tariff system should be checked

CHAPTER IV

QUOTAS IN MODERN COMMERCIAL TREATIES

To attempt a detailed analysis of the working of the quota system in different countries would be beyond the scope of the present chapter This is so because the effects are so marked and varied in details that even a succinct review would be much beyond the ambit of an ordinary chapter On the other hand, a brief discussion of the bases of the quota system would be much more valuable, because in matters of principle most of the important features are common to the system as a whole, the differences are confined primarily to matters of details needed to suit the local requirements of different countries As regards the importance of the subject, it may be noted that the quota system has altered materially the structure of commercial treaties to merit special study It has obstructed the flow of international trade more effectively than the tariffs In the present chapter, therefore, we shall study the general economic implications of the quota system and its effects upon the technique of modern commercial policy

The Circumstances which led to the Adoption of the Quota System—An analysis of modern commercial policy reveals that the quota system is extensively used by the European countries and the United Kingdom, it has become an integral part of their commercial policy [1] In other countries, too, the quotas are used for regulating international trade, but their use is sporadic It is significant to note that France gave the lead in the adoption of the quota system in 1931 Probably France would have resorted to the quota system earlier, but she was fortunate in not having felt the

adverse effects of the depression in the earlier years due to her relatively lower cost structure With the continuous and steep fall of prices in other countries, however, the French industries and trade began to feel the competition of foreign imports France, having stuck to the gold standard, became a profitable market for foreign producers to sell their goods, with the result that the French imports increased At the same time her exports recorded a sharp decline due to her higher cost structure and the tariff barriers raised in the export markets The trade balance, normally deficitary, grew more so to an alarming extent[1] It may be noted that the French tariff of 1927 was not protectionist in the sphere of agriculture But, with the beginning of the world crisis the French Government promptly raised the customs duties in December 1929 and in April 1931, the most prominent being those on corn, flour, livestock, meat, milk products sugar and wine No wonder, therefore, if the commodities like wheat, maize, barley, port, sugar, etc, had to pay extremely high duties[2] These increases in the customs duties, however, could not render any material assistance to the French industries and trade, because 70 per cent of the French tariff duties were consolidated in commercial treaties and extended to about fifty countries by the Most-Favoured-Nation Clause The Franco-German treaty of 1927 was the basis of the network of commercial treaties which fettered the French Government from making an effective use of the customs tariff in restricting the flood of imports Germany, naturally, refused to agree to the cancellation of this treaty Escape from the obligations of the Most-Favoured-Nation Clause had to be found France, therefore, resorted to customs quotas, which proved more effective than tariffs in regulating its trade

Britain Adopts Import Quotas.—Similarly, Great Britain adopted the quota system to protect her agricultural interests It has already been shown that as a result of the Great War and its aftermath there grew up a general con-

1 Vide Jones, J M: "Tariff Retaliation," p 140 and Haight F A.: "French Import Quotas," pp 8-9

2. Vide, Liepmann, II: p 65.

sensus of opinion that a prosperous rural community was essential for the healthy growth of the economic and social structure of any country, no matter how advanced were its trade and industries A well-balanced and broad based economic and social structure was needed Further, with the setting in of the depression there came a catastrophic collapse in world agricultural prices which strengthened the hands of the protectionist elements in Britain A number of schemes have been formulated to promote the expansion of agriculture in Britain Of the several devices used to help the British agriculturist, import quotas are very important

The primary objects of this new policy are to protect the British agriculture from the heavy flood of imports at very cheap prices, and to stimulate the revival of British farming on a sound and permanent basis Thus, the measures taken may be broadly sub-divided into two categories (1) those of an emergency nature and (2) of a permanent character The policy of Imperial Preference has further added to the complications Emergency measures are calculated to restrict food imports for economic as well as non-economic reasons The long-term measures attempt to improve the efficiency of British agricultural production

In the initial stages tariff duties were raised on foreign imports of agricultural products to protect British agriculture The Import Duties Act of 1932 imposed a ten per cent ad valorem tariff on all foreign imports, with certain specified exceptions, the chief agricultural products on the free list being wheat, maize, meat, livestock, wool, hides and skins The duties were further raised on fresh fruits, vegetables and flowers, potatoes, oats, barley, condensed milk, preserved fruits, canned vegetables and poultry The Ottawa Trade Agreement of November, 1932, raised still higher the duties on non-Empire imports of agricultural produce To certain branches of British agriculture protection was extended against the Empire as well as non-Empire imports Of the commodities thus protected,

the more important were meat, dairy products, eggs, and poultry.

Tariffs failed to provide an adequate protection to the British farmer under the exceptional circumstances of the world depression Of the supplementary measures devised to help the agricultural interests quotas are very important Meat, milk, hops eggs and poultry have been subjected to import regulations under the Agricultural Marketing Act of 1933 These import quotas have been regulated partly by the unilateral decision of the British Government, and partly by the negotiation of trade agreements with other countries or by other countries voluntarily restricting their exports to Great Britain

German Quota Regulations—In the structure of German trade and industries forces had become sufficiently strong by 1929 which emphasised the necessity of self-sufficiency, in respect of agricultural requirements such as corn production, live-stock raising meat production, dairy products, and sugar In 1929 the German Government compelled the German consumers to absorb the whole home output of cereals and imports were to be permitted only when the supply of German grains failed to provide for the essential needs Tariff duties have been used to keep the home price at a definite level Import of wheat and rye have practically ceased as a result of protectionist measures The duties on pigs and cattle were raised The meat imports were also subjected to higher duties In 1932 the imports of butter were subjected to quota regulations in addition to duty increases and currency restrictions The consumption of these commodities has been rigidly regulated

Other European countries also resorted to the import quotas to protect their agricultural population Non-European countries also took to quota regulations From a critical analysis of these regulations in different countries it becomes clear that tariff as an instrument of regulating undesirable imports proved inexpedient and had to

be supplemented by some more effective, expedient and efficient device The quota system could claim all these advantages Import quotas are said to be supple, simple and swift

Started as an emergency measure, the import quota system has come to be recognised as an accepted form of trade control For the purpose of the present study an import quota system may be defined as the limitation by quantity, weight, or value of imports of a commodity for a specified period of time by legislative enactment or legislative decree Therefore, an import quota needs to be distinguished from a customs or tariff quota Under the former physical quantity of imports is fixed, while in the case of the latter, a fixed quantity of imports can enter at a certain favourable rate of duty and the additional amount is called upon to pay a higher rate We are concerned primarily with the import quota

Implications of the Quota System—The restrictions on imports are apt to cause a rise in the prices When the restriction takes the form of an import duty, this additional burden has to be borne by someone In the first instance, the importer is called upon to pay the duty to the customs authorities But the burden may be borne either by the importer, or by the exporter, or by the consumer, or by all the three parties The burden on the importer can be only temporary In the long run he must be relieved of the burden or else he will move to some more remunerative employment and the imports will cease This will happen only when the duty is proved to be prohibitive Under normal circumstances, the importer will try to transfer the burden either to the exporter or to the consumers In the former case the exporter will have to charge a lower price to the importer in proportion to the duty levied and thus bear the burden In the latter case, the importer will charge a higher price to the retailer, and through him the consumer, who will thus have to bear the incidence of the duty The importer must have his reasonable and fair profits

prices This creates disparities between the domestic and foreign markets, similar to those created by the imposition of customs duties, with the essential difference that whereas in the case of import duty the disparity is limited by the incidence of the duty, in the case of import quotas there are no such known limits[1] The import quotas definitely limit the foreign supplies and no price adjustment can help to bring about an equilibrium between the demand for and supply of foreign commodities except the substitution of home for foreign production The actual extent of the rise in the internal price level will depend upon the ease and extent of the substitution of domestic for foreign supplies

The disparity in price structures creates a *national* market, for goods and services subject to quota regulations, distinct from the international market, and more favourable *to the domestic producer The result is that* the *domestic* industries and trade get marked encouragement At the same time, the imports permitted under the quota system get the advantage of higher *internal prices This extra* advantage will be pocketed exclusively by the exporter if he has made his own arrangements for selling the goods in the protected market, within *the authorised limits* through his own agents In case, however, the domestic importer himself makes purchases in the foreign countries concerned he pays them a competitive price *in those* markets and thereby keeps to himself the difference between that and the price charged in the domestic market The latter alternative is more favourable to the quota imposing country and therefore instances are not lacking where definite encouragement has been given to foster this trend

The license system is an essential part of quota regulations, the imports are permitted only subject to license,

in order to prevent abuse or evasion. The licenses have to be issued for permitting the imports within the prescribed limits. Therefore the holder of the license is in a position to secure for himself the difference between the foreign and domestic price. The distribution of import licenses may take one of the two forms. The licenses may be distributed amongst the traders within the importing country,[1] so that those who hold the licenses alone have the authority to buy the goods in the foreign market and import the same. In this event the importer can take full advantage of the competition between the foreign sellers and pay a relatively lower price to them. Thus, he succeeds in keeping to himself the difference in prices. If, however, the licenses are distributed amongst the foreign manufacturer, who may have their own selling organisations in the importing country, they will pocket the difference in prices or else charge the domestic importer the price prevailing in the protected market, less the costs of the importer, as they are the sole supplier of the goods. This second alternative is at times adopted to allay the suspicion of discrimination[2] in foreign countries, by permitting them to distribute the quota amongst the manufacturers in their own country, with the understanding that the imports will be evenly distributed throughout the year.

Thus, the effects of the quota regulations are essentially different from those of the tariffs. The incidence of the import duty is well diffused throughout the economic system and new equilibrium is established which keeps the entire system in full working order without any serious dislocations. The import duty raises the price level in the protected market and by altering the equilibrium of demand

1 "Where there are no allocations, it is important for the importing country to issue licenses to importers as a regulatory factor in order to control quality and fair distribution of contracts among domestic importers. This is best achieved by the creation of an issuing body composed of representatives of merchant importers and producers with power to distribute the licenses to former importers, usually according to the percentage their former imports bore to the total imports of the designated commodity although some provision should be made for new traders." Vide, Dietrich, E. B. *World Trade*, p. 112.

2. Although this frees the importing country from the onus of favouritism, it has been criticised as giving to the foreign organisation which distributes the licenses, the power to choose quality and types of specific imports difficult to define unless standardised. It may also be detrimental to established importing houses.

and supply helps to distribute the incidence of taxation among the producers, traders, and consumers Of course, the larger share of the burden is borne by the consumers It is, however, essential to note that the import duty affects all producers, traders, and consumers, not only of the commodity taxed, but also of all related and competing products The effects are spread over the producers, traders, and consumers of a large variety of commodities in a number of countries No wonder, therefore, that under a normal protectionist tariff the disparity between the national and international price systems is not very wide The adjustments create a new equilibrium and thereby keep the economic system free of violent upheavals To create wide and unbridgable gap between the prices of the same commodity in the protected and free markets the tariff needs to be very high The quota system however, directly and definitely limits the imports of particular commodities and no price adjustment can alter the same The obvious result is marked disparities in the price levels of different countries

Objectives and Motives of an Import Quota System—It has already been emphasised that the fundamental aim of the quota system is the effective and prompt regulation of imports The need for restricting imports may be dictated by several considerations

(1) **To Regulate the Balance of Payments or the Trade Balance**—The French quota system had this objective at its inception Of the advanced industrialised countries France was fortunate in escaping the adverse effects of the world depression in its earlier stages because she had undervalued the franc when reverting to gold standard after the Great War As a result of this undervaluation the costs of the French industries were low as compared with those of the other countries But, with the catastrophic fall in world prices, which the depression brought in its wake, the advantage enjoyed by the French industries was soon neutralised, and imports into France began to increase This tendency got strengthened as France

decided to stick to the gold standard in face of devalued and managed currency systems of her competitors. Thus, whereas the French imports increased, her exports experienced increasing difficulties due to high cost of production, decrease in demand, rising tariff barriers, etc. The normally deficitary French trade balance grew more so. This state of affairs demanded drastic and prompt remedy. The tariff duties failed to relieve the situation due to the consolidation of 70 per cent. of the duties under commercial treaties. The quota system was, therefore, enforced to regulate the balance of trade.

(ii) To Assist or Protect Specific Industries.—Another important objective for which the quota system has been used is to assist definite industries. This assistance may take the form either of encouraging exports or of restricting competitive foreign imports. The British quota system is an instance in point. Great Britain has adopted the quota system to encourage, *inter alia*, the exports of British coal, iron and steel, and textile industries. Several trade agreements have been concluded, based on the quota system, to increase the sales of these products. For instance, the Trade Agreement with Denmark, signed in London on April 24, 1933, contains specific provisions guaranteeing the Danish market for British coal. Under the Protocol the Government of the United Kingdom has the right to terminate the agreement with three month's notice if in any one year the amount of British coal imported into Denmark is less than 80 per cent. of the total imports of coal into Denmark in that year.[1] Thus, 80 per cent. of the Danish market is secured for British coal.

The Trade Agreement with Norway and the Protocol attached thereto, signed in London on May 15, 1933, also provided concessions for British coal. Under the Protocol, the British Government has reserved the right to terminate the Agreement at any time upon three months' notice if in any period of twelve months the amount of British coal

[1] Vide, B. T. J., 27-4-1933, pp. 644-49.

imported into Norway is less than 70 per cent of the total imports of coal [1]

The Trade Agreement with Sweden and the Protocol attached thereto signed in London on May 15, 1933, secures a definite share of the Swedish market for British coal The Protocol empowers the British Government to terminate the Agreement upon three months' notice if within any one year the imports of British coal into Sweden are less than 47 per cent of the total imports of coal [2]

Similar trade agreements were entered into with Iceland, Estonia, Finland Lithuania and Latvia The Trade Agreement with Iceland secured 77 per cent of the Iceland market for British coal [3] Under the Anglo Estonian Agreement the British Government has reserved the right to terminate the Agreement if in any one year the amount of British coal imported into Estonia is less than 85 per cent of the total imports of coal or if it is less than 35 000 metric tons [4] The Agreement with Finland reserved 75 per cent of the total market for British coal The Lithuanian Agreement provided that the British Government shall have the right to terminate the Agreement if in any one year the amount of British coal imported into Lithuania is less than 80 per cent of the total imports of coal or less than 178 000 metric tons, or, if the amount of British coke imported is less than 50 per cent of the total imports of coke [5] The Latvian Agreement secured 70 per cent of the market for British coal [6] The Danish Agreement reserves 80 per cent of the market for British coal [7]

The Anglo French Trade Agreement of June 1934 is interesting The Agreement provides that as regards the imports of coal into France falling under the normal quota the French Government agreed to guarantee the existing percentage for import of British coal With regard to

supplementary allocations the French Government agreed that during the continuance of the present agreement, (1) in the event of the global quota being reduced, these supplementary allocations shall not be reduced in a greater proportion, and (2) these supplementary allocations shall continue to remain open to free competition [1]

From the foregoing illustrations it is clear that the British Government has used the quota system to encourage the exports of British coal Similarly, the British trade agreements contain specific provisions for the encouragement of other British exports to countries levying quotas Thus, the Anglo-French Trade Agreement provides that in connection with quantitative restrictions on imports into France, the French Government guaranteed that the United Kingdom will be accorded a full share of all quotas in regard to any class of goods, whether existing or to be established hereafter The share should not be reduced,[2] whether the global quota be increased or reduced [3] Further, the British industrial products which were subject to quota regulation before January 1, 1934, on their importation into France, and which formed in 1931 less than 10 per cent of the total imports into France, their quantities should not be reduced

The Government of Estonia, according to the Trade Agreement, agreed not to impose any import restrictions on those articles enumerated in Parts I and II of the First Schedule which were free from restrictions As regards those articles enumerated in the said Schedule which were subject to import restrictions, the Estonian Government agreed to operate the restrictions in such a way as to permit the benefits in full to accrue to the goods Further, it was agreed that the imports into Estonia of goods not enumerated in the said schedule should in no case be restricted below those of the year 1933 If the Estonian Government decides to impose import restriction on goods

which are hitherto free from restrictions and are not covered under the First Schedule, the British Government shall be consulted[1] Thus, the uncertainty and the rigour of quota restrictions on British exports has been substantially minimised The future course of import restrictions has also been controlled within certain limits

The quota system has also been used for protecting specific industries against the inroads of competitive foreign imports The new agricultural policy adopted by Great Britain since the depression affords the most striking illustration of the use of quota regulation for restricting the imports with a view to fostering the growth of particular branches of domestic production The expansion of British agriculture had to be encouraged in the interests of economic as well as political expediency The flood of imports at abnormally low prices during the initial stages of the world depression caused alarm amongst the British farmers who could not face this menacing competition It was, therefore, felt that those branches of British agriculture which could hold their own in normal times should be protected during this emergency Of the several methods used in this new technique of protection quotas are important

Great Britain entered into trade agreements with several countries which contained quota regulations for protecting certain branches of the British agriculture From these agreements it is clear that the British Government had substantial latitude in fixing the specific quotas, although conditions were imposed in several cases and minima fixed Therefore, the British Government has pursued the policy of stabilising the supplies of certain commodities on the British market on an estimated average of certain pre depression period The domestic producers are encouraged by several devices to extend their output and secure to themselves greater portion of this market With this object in view, the estimates of the domestic output

able imports by quota regulations and thereby compel the exporting countries to make equivalent concessions Thus, quotas can be used as an aid to commercial reciprocity It is interesting to note that both Great Britain and France have made full and frequent use of the quota system for this purpose Great Britain, till the inception of the depression, had been largely a free trader, and as such an importer of foodstuffs and raw materials on a huge scale, which gave her considerable bargaining power to meet the new situation With the setting in of the depression, Great Britain found her domestic markets flooded with foodstuffs at low prices and her foreign markets for manufactured goods rapidly declining The problem facing the country was, therefore, two-fold to protect the British farmer against uneconomic foreign competition in the home market, and to provide the British manufacturers more stable foreign markets The objective of British commercial policy since the Ottawa Trade Agreements has, therefore, been to protect the British farmer and provide outlets for British industries Within the Empire, excepting India and other dependencies, Imperial sentiment has been fully exploited to secure maximum advantage to the British industries in return for certain concessions in the British market for agricultural products of the Dominions "The primary objects of the new policy are to protect British agriculture by emergency measures from being overwhelmed by the threatened flood of imports at ruinously low prices during the depression, and to stimulate a revival of British farming under conditions which will ensure its permanent welfare Subject to these objects being achieved, Empire countries are to be given preference over foreign countries in the British market, in other words, the Ottawa principle is to be applied, the interests of the home producer coming first, Empire producers coming second, and foreign countries last."[1] Subsidies, levies, organised marketing, tariffs and quantitive regulations have been used to encourage British agriculture and the remainder of the market is used for bargaining with the Empire and

non-Empire countries so as to find suitable outlets for British manufactures Definite quotas have been allotted to foreign countries, like Argentine, Denmark, Sweden, Norway, Iceland, Germany, etc, in respect of certain agricultural products, in return for British coal and manufactures

The French quota system has also been used for commercial bargaining Finding 70 per cent of her tariff consolidated under commercial treaties containing the Most-Favoured-Nation Clause France found herself considerably fettered in protecting her trade and industries from increasing foreign competition Germany was unwilling to denounce the Franco-German commercial treaty on which the entire network of commercial treaties was based Under the circumstances, France wanted tariff liberty so as to secure commercial reciprocity and this she was able to do with the assistance of quota system Mr Jones says[1] that France wanted to create a barrier against importation behind which the Government could proceed with the denunciation of her most-favoured-nation treaties, to secure tariff liberty, and to proceed with the negotiation of new treaties strictly on the basis of mutual concessions, abandoning the unconditional Most-Favoured-Nation Clause

(v) To Plan Trade on Barter Basis—Quotas are used to plan trade on barter basis or to effect exchange of specific commodities By this method an attempt is made to effect exchange of specific goods in which the countries concerned are interested on the basis of reciprocity The Indo-Japanese Trade Agreement illustrates the use of quota system with this objective

The Swiss and the German Governments follow similar *lines of action, the quota system has been so used as to* reduce the trade to crude barter During 1930-31 Switzerland suffered acutely from rising tariffs, quotas, and exchange controls all over the world In this connection

1 Vide Tariff Retaliation pp 142-46 Haight F A z French Import Quotas," pp 104-11

the decree-laws issued by the Brunning Government in Germany in 1931 are significant, since they raised the tariffs on certain agricultural and industrial products to fantastic levels These high tariff barriers affected adversely the Swiss export trade to Germany. This was not all Germany, in addition, resorted to aggressive trade promotion, which almost doubled her exports to Switzerland This form of German commercial policy caused alarm amongst the Swiss people The Swiss Government, therefore, requested the German Government to modify her trade restrictions, but the latter refused to change her policy. Thereafter Switzerland also changed the technique of her commercial policy to defend her trade and industries, she wanted reciprocity Of the several devices used to achieve this purpose, the system of exchanging specific quotas is significant

The Italian-Soviet Commercial Treaty has similar quota arrangements Italy purchased from Russia large supplies of wheat and oil, as well as coal and wood, while Italy furnished to Russia stated amounts of automobiles, aeroplanes, ships, motors, industrial and agricultural machinery, and chemical products The first treaty alone provided for an exchange of 2000 Fiat Trucks for a certain amount of Russian wheat[1]

(vi) **Use of Quotas for Retaliation**—Quotas have also been used for retaliation As an instrument of retaliation, quota system has been extensively used by countries like Italy, Germany, Switzerland, etc Italy and Germany have used this instrument of retaliation more frequently and effectively The democratic countries have also tried to use this instrument to enforce reciprocity For instance, the Swiss Government regulates trade through the Department of Public Economy, which outlines the measures of reciprocity, to be carried out by different committees of which importers are members Thus, the State regulates and determines the trends of trade, rather than the free will of the importers

(vii) *Use of Quotas for Reducing Tariff Barriers.*—Another important objective with which the quota regulations may be imposed is to lower the tariff barriers For instance, Switzerland found, as a result of growing trade restriction and aggressive commercial policy adopted by foreign countries, her export trade rapidly declining and imports recording a striking increase The total Swiss exports declined from 2104 million francs in 1929 to 1348 million francs in 1931 A detailed analysis of Swiss exports is more interesting The exports of foodstuffs fell from 177 million francs in 1929 to 122 million francs in 1931, cotton goods from 235 million francs to 135 million francs, silk goods from 298 million francs to 198 million francs, watches and parts from 277 million francs to 143 million francs, machinery and apparatus from 309 million francs to 200 million francs during the same period [1] This alarming fall in the Swiss exports was found to be due to rising tariffs, quotas, and exchange controls all over the world The Swiss Government had, therefore, to protect her trade and industries from this menace and find markets for her products The new Swiss commercial policy, which has developed since 1931, incorporated quota regulations to secure reduction in the trade barriers against her products on the basis of reciprocity

(viii) **To Make International Export Agreements**—Sometimes international agreements are negotiated for regulating the export trade in specific commodities on a quota basis Specific export quotas are assigned to important exporters of commodities concerned Wheat and sugar agreements are of this nature The exports of different countries are definitely restricted to the quotas assigned to them

The tea restriction scheme and the export quotas allotted to each country concerned is the most successful example The initiative in the direction came from the producers, but the governments of important countries concerned—India, Ceylon, and Netherlands Indies—sanctioned the

1 Vide Liepmann, p 270

scheme and gave it the force of law On the first of April, 1933, when the five year control plan was adopted, the countries covered under the scheme supplied about 80 per cent of world exports of tea Each country was assigned a specific export quota Similarly, the International Rubber Regulation Agreement was put into force from 1st June, 1934, for a period of four years and six months, and was later on extended for five years to 1943 In 1936, this Agreement controlled 97 per cent. of the crude rubber export Tin is another important commodity which has been brought under international government control The present agreement was ratified on January 5, 1937, to last for five years

(ix) To Check the Flood of Imports Pending Tariff Legislation.—Quotas, essentially temporary, are at times used to check the flood of imports pending tariff legislation Cases are not uncommoon where in anticipation of a particular legislation pending before the legislature of a democratic country the exporters interested in the commodity have *increased* their *exports* to escape the *additional* taxation To neutralise these undesirable activities quota regulations are imposed during this period of transition

Technique of Quota System:

Source of Authority.—To be effective, quota regulations should be promptly enforceable Therefore, the executive is usually empowered to decide[1] the nature of the import quotas to be permitted and their method of enforcement This enables the Government to regulate the trade in time and check effectively the undesirable forces taking undue advantage of the situation Being an emergency measure, the executive is the sole judge of the quota regulations To safeguard against the power being abused by an inexperienced bureaucracy, the legislative check is imposed in the form of ratification

Unit of Import Quotas.—The unit for imposing quotas may be either quantity, weight, or value, or a combination of all three. The selection of the unit to be used will depend upon the objective of the quota system and the nature of the commodity concerned. For instance, value can be a more effective and efficient unit where the objective is to adjust the balance of payments[1] or to maintain the internal price level. If, however, the purpose of the quota system is to assist or protect specific industries against the flood of undesirable imports, value as an unit would be inefficient and ineffective. Here quantity would be more effective, since it would put a definite limit on imports.

Base Period for Determining Quotas.—In fixing quotas the usual practice[2] is to choose a base period, either a year or an average of few years or a specified period of a single year or group of years.[3] This base period differs with different countries and in the same country with different articles. The determining factors are the economic conditions of the countries and the nature of the article. There can be no uniformity in selecting the base period. It is apt to result in discrimination[4] and injustice[5] to the parties concerned.

Quota Period.—In fixing quotas it is equally essential to specify the period during which the imports, in quantity or value, of a given commodity are to be permitted. The period to be selected may be a year, a quarter, a month, or a week. The length of the period varies with the type of the commodity, the purpose of the quota, and the need for flexibility. The customary periods are a year, or a quarter. In the case of perishable commodities, however, an annual or quarterly quota may be divided for the sake

1. The Anglo-Italian Commercial Agreement of 1936 contains quota provisions based on value. Vide B. T. J., 1-11-1936, pp. 70?-70?.

2. The sole important exception is that of quotas established primarily for bargaining.

3. The base periods are used as an index of normal consumption of the product to be put under quota and to provide an equitable method for the distribution of quota allotments among importing countries in order to avoid discrimination.

4. It can be used to observe favouritism by selecting a base period during which trade with desired countries was especially favourable.

5. Past consumption is not always a reliable gauge of future consumption, nor may past or future supply markets be always desirable.

of convenience into monthly or weekly allotments An annual quota offers greater certainty to both importers and domestic producers and checks sudden fluctuations in cost and price structure Further, adjustments in the technique of production can be better effected and waste minimised The quarterly quotas, however, permit the Government to so regulate the imports as to suit the variations in seasonal requirements But, the producers of the commodities subject to quarterly quota regulations find their markets in constant flux, which impairs their efficiency, and leads to waste

Allocation of Quotas:

(i) ***The Global Quotas.***—The methods of allocation of quotas vary In some cases the country applying quota regulations fixes the permissible total amount or value of the imports of a commodity, from all countries, and does not make any further allocations between different countries In this case all countries are permitted to compete among themselves This form is known as Global Quota Under these regulations, the importers may import from any country and in any amount until the quota is filled up, without any import authorisation This method enables the importing country to take full advantage of the competition amongst the producers in different countries Besides, it does not discriminate between exporting countries

In its working, however, this system has given rise to considerable administrative difficulties The authorities find it very difficult to know how much of a given commodity has been imported from each customs house from day to day, with the result that often quota limits are exceeded before the imports can be checked Further, general experience has shown that immediately after the announcement of a new quota, or at the beginning of a new period, large quantities of goods are rushed across the frontier of the country before the quota is exhausted This has spurred speculative elements

(ii) **The Unilateral Quotas.**—To eliminate the waste resulting from the global quota system unilateral quotas are imposed. Under this system the administrative authorities fix the total quantity or value of imports and allocate it amongst the different countries These quotas are called unilateral because they are fixed without consulting the exporting countries The amount allotted to each country is determined by the average imports of the base period To check the tendency of imports exceeding the quota figure and speculation amongst dealers the import license requirements have been attached to the quota system.

(iii) **The Bilateral Quotas.**—Another important method is to allocate quotas as a result of bargaining with each exporting country Thus the suspicion of discrimination is minimised. Besides commercial reciprocity as a basis of quota restrictions removes the rigidity of administration The shipments of goods are more evenly distributed throughout the quota period which limits the scope for speculation Further as the arrangements incidental to the quota regulation are determined by mutual agreement commercial relations are well maintained. These quotas are better adapted to the needs of the parties concerned because during the process of negotiation producers of both the countries are taken into confidence

Entry Regulations.—Enforcement of quota regulations has given rise to difficulties In those cases where the quota is not distributed among exporting countries and no import authorisation is required the flow of imports has been erratic and caused considerable industrial dislocation This is a primitive and most irrational method To remove this inconvenience quotas are usually allotted to different countries and the entry is permitted subject to license

The licensing system, which was extensively used during the Great War has been successful in regulating the flow of imports Special Committees have been entrusted

with the task of distributing licenses among the importers of standing in proportion to their imports in previous years [1]

Licenses are issued after adequate investigation about the importer, his imports in the previous years, the quality of the goods he seeks to import, etc In some cases, the importer is expected to supply the sample of the goods to be imported, and the Committee on granting the license, sends one of the samples to the customs house through which the goods have to be imported The license usually specifies the customs house and the period within which the commodity should be imported The license is non-transferable Sometimes the license fee is levied to meet the expenses of the licensing authority and to appropriate a part of the profits arising from the quota restrictions

This method of distributing licenses favours the old established merchant houses at the cost of less known and new entrants It creates vested interests and encourages monopoly Further, competition tends to be eliminated, and the evil of speculative purchases is encouraged The administration is dilatory and costly

Sometimes, the distribution of licenses (or export certificates) is entrusted to the foreign Government or to some producers and exporters in foreign countries, to remove the suspicion of discrimination This practice has created further complications Numerous organisations of exporters and importers have grown up and have changed the structure of distributive trade

Quotas and the Structure of Commercial Treaties—The structure of commercial treaties has undergone marked changes with the inception of the quota system We have seen that quotas have become an integral part of modern commercial treaties As a result of the incorporation of quotas and other restrictive measures in the commercial treaties international trade is being diverted in artificial

channels and rigid and narrow and bilateral balancing of trade has become a rule. Substantive bilateralism is in vogue. This development in commercial policy has exerted a profound influence on the character and channels of trade and the future seems to promise further complications in this direction. That this bilateral balancing of trade on quota basis has restricted trade is too self-evident to need detailed proof. Trade is essentially multilateral. The waste and inefficiency which this instrument of commercial policy has bred through its inroads upon the international division of labour and seeks to nourish, has further aggravated the malady its sponsors expected it to cure.

The quota system has become more important than tariffs as a method of commercial bargaining and divested the Most-Favoured-Nation Clause of its efficacy in securing equality of treatment. The assumption is that quotas do not fall within the ambit of the Most-Favoured-Nation Clause. In the pre-depression period, commercial negotiations generally followed primarily the method of bargaining on the basis of tariff schedules, and the tariff reductions agreed to were extended to other countries under the Most-Favoured-Nation Clause of the treaty. Thus, international trade was essentially triangular and free scope was permitted to forces of competition, which helped to effect prompt adjustments in cost and price structure. The quota system obstructs these adjustments by the most effective restrictions on imports.[1] In fact, the Most-Favoured-Nation Clause has become largely ineffective as a result of the quotas being incorporated in the commercial treaties and increased specialisation of customs classification. The principle of equality of treatment thus gives way to discrimination, for under the quota regulations discrimination is very difficult, if not impossible, to avoid.[2] Discrimination may be reduced if quotas are established in such a way as not to modify the competitive

1. "The fixing of import quotas, like the fixing of maximum prices, is an interference with the price mechanism which is alien to the price system." Prof. Haberler G. "International Trade" p. 348.

2. All the three possible formulae savour of discrimination. Vide, Haight, F. A., "French Import Quotas," p. 93.

position of other countries on a given market But there are considerable practical difficulties in fixing such quotas In fact, no system of quantitative regulations of imports can fulfil these requirements In short, a system of quantitative limitation must breed discrimination, which is a direct antithesis of the Most-Favoured-Nation Clause

In the modern commercial treaties we find the Most-Favoured-Nation Clause side by side with the quotas These quotas, instead of being fixed according to the proportion of particular imports to the whole over previous years, have been granted on the basis of reciprocity to the countries offering corresponding advantages M Sarrant declared in November, 1933 "The quota system must be made an instrument for directing French purchases to those countries which offered the best market for French products"[1] With this object in view, commercial treaties have been negotiated with different countries, and quotas fixed as a result of bargaining These quota arrangements differ with individual countries and have not been generalised with the Most-Favoured-Nation Clause For instance, under the Supplementary Agreement[2] attached to the New Commercial Convention between France and Spain, entered into on March 6 1934, France granted to Spain 100 per cent quotas for certain agricultural products, wood, twisted cotton yarns, bananas, cotton socks and stockings, certain varieties of leather, etc, and increased quotas for certain fresh, preserved and dried fish Spain also received separate quotas for fresh trout, women's clothing certain varieties of paper razor blades, etc, in respect of which she had previously shared in the quotas allotted to other countries

Spain in its turn, granted to France, a fixed proportion of certain quotas which have been or are to be established, viz, (i) France is granted a quota of 100 per cent of her average imports for the last three years of charcoal, unmanufactured tallow and other animal fats, a quota of 80

In the earlier years the administration of the quota system was relatively flexible and liberal, with the result that actual imports were often more than the amount fixed by the higher authorities In France, which gave a lead in introducing this system it was found that in 1932 imports were about 86 million quintals, whereas if the system had been rigidly applied to all goods they would have fallen to about 32 million quintals[1] Since 1933 the restrictions have become more stringent, with the result that imports have fallen considerably For instance, French imports of horses fell from about 55 thousand in 1931 to 7 thousand in 1934, cattle from 724 413 quintals to 54 498 quintals pigs from 415,951 quintals to 68 447 quintals, meat (fresh and chilled) from 382 424 quintals to 48,636 quintals, meat (frozen) from 664 633 quintals to 229 666 quintals, eggs from 306,824 quintals to 120,059 quintals, cheese from 375 624 quintals to 159,641 quintals, and butter from 185 234 quintals to 43 562 quintals during the same period[2] The agricultural interests constitute a strong political force in France and it is due to the pressure exercised by them that the import quotas were extended to cover all the important products of field and pasture

The British agricultural quota system has also restricted imports, particularly from the non-Empire countries Between 1931 and 1934, imports of meat from non-Empire countries declined by about 30 per cent, of wheat and flour by 33½ per cent, eggs by 26 per cent, vegetables by 60 per cent and fruits by 70 per cent This reduction in imports was, however, made up by the rise in imports from the Empire countries[3] The British imports of potatoes declined from 22 2 million cwts in 1931-32 to 3 2 million cwts in 1933-34[4] The imports of Danish butter into U K declined from 123 000 metric tons in 1931 to 109,742 metric tons in 1936[5]

Similarly, the quota regulations introduced in other advanced countries have also restricted trade The import quotas levied by the United States[1] on sugar, cardage shingles etc have had their restrictive effects The protection thus extended to American sugar interests was in excess of anything ever achieved by the Republicans 'It is highly probable that recent experience will then be drawn on to extend the quota system in a much more restrictive manner The opening wedge has been driven and no one can say how far the use of quotas will proceed. It is quite possible that instead of further general upward revisions of the tariff the future will see a broad extension of the quota system If this should happen we shall have paid dearly for any benefits the system may have conferred in recent years "

Industrial Quotas—The circumstances which led to the imposition of industrial quotas and their objectives were different in essential particulars from those of agricultural quotas Looking to the French import quota system we find that imports of food produce into France had increased by about 50 per cent the French market was flooded This flood had to be regulated On the other hand the imports of manufactured goods into France in 1931 had actually declined The French industrial quotas were therefore adopted to "aid in the task of reducing the import surplus to total trade to reserve a larger part of the French market for home producers who were suffering from declining exports and to stop the inflow of certain goods at declining prices'[3] In their working the industrial quotas have helped the domestic manufacturers considerably by reserving a larger share of the home market for them The objective of restricting imports and redressing the trade balance with certain countries has also been realised For instance the adverse balance of trade with Germany which was about 3 782 million francs in 1930 was reduced to 239 million francs in 1934[4]

1 Vide Whittlesey C R "Import Quotas in the United States," Quarterly Journal of Economics, November 1937 pp 37-65
2 Ibid, p. 63
3. Vide Haight: "French Import Quotas" p 55
4. Ibid, p. 60.

The restrictive effects of the industrial quotas on the volume of trade have been proved from the experience of other countries as well As a result of quota restrictions imposed by Switzerland we find substantial reductions in her total imports The German exports to Switzerland dropped in 934 to 54 per cent of 1931 [1] French exports to Switzerland declined by more than 40 per cent between 1931 and 1933 [2] Holland adopted import quota restrictions in 1932 with the result that her imports have declined considerably For instance German exports to Holland fell to 482 millions which was about 50 per cent of the value of 1931 [3] Czechoslovakia adopted import quota system in 1932 and her imports fell rapidly German exports to Czechoslovakia represented only 38 per cent of 1931 figure [4] Thus the quota system definitely restricts trade

Import restrictions affect adversely the export trade of the country resorting to them This influence is exerted chiefly through three channels its effec s upon purchasing power abroad its tendency to maintain internal prices and the measures of retaliation which other countries are likely to adopt [5] As for the first it is essential to remember that our ability to export is determined by our willingness to import exports pay for imports Besides the portion of the supply excluded by the import quotas is sold on other markets at reduced prices which tends to restrict the foreign demand for the goods of the quota imposing country The benefits of triangular trade are neutralised Secondly tre quotas have tended to aggravate the difference between domestic and world prices For instance quota restrictions imposed by the United States on import of Cuban sugar have created a wide disparity between New York and world prices Before the imposition of the quota system sugar prices in the United States were equal

to world prices plus the tariff on Cuban sugar This relationship has been distorted after the imposition of quotas and impaired the flexibility of New York prices This increases the difficulties of the exporting industries No doubt higher internal price level stimulates domestic industries, and leads to the displacement of imports by local produce, but the higher cost of production of local industries, resulting from higher internal price level, handicaps them in foreign markets These difficulties of the exporting industries increase much more if they produce luxuries Thirdly, retaliation by foreign countries is inevitable when a country resorts to quotas, rigid and restrictive These retaliatory measures will be more far-reaching and effective on goods having elastic demand.

Conclusions.—The import quota system is one of the most outstanding features of the technique of protectionism developped during the depression It marks an important development in the technique of modern commercial policy Import quotas are distinctly superior to tariffs as protective and defensive devices When countries feel the necessity of quick, certain, and drastic reduction of imports, they resort to quotas, which enable them to achieve this result more easily and effectively than the traditional device of tariffs Quotas are also more flexible than tariffs They have a distinct advantage, both in respect of effectiveness and flexibility, over tariffs as an instrument of commercial bargaining These characteristics of the import quota system have made it a most useful instrument of commercial policy to tide over an emergency

The use however, of import quotas as a permanent instrument of commercial policy in normal times is undesirable and uneconomic Under normal economic conditions, customs duties are far more useful instruments of protection than import quotas No doubt, the tariffs do interfere with the free and full functioning of price competition in determining the flow of international trade, but a reasonable and moderate protectionist tariff, far

from desrtoying it, does not even seriously impair the functioning of price mechanism Under a moderate protectionist tariff, there is sufficient scope for the play of the forces of competition to determine the structure of prices in the protected market, whereas import quotas effectively check competition in the import trade

By the substitution of import quotas for customs duties the executive has usurped legislative functions This usurpation of legislative function has made the executive more irresponsible to the people in formulating its commercial policy Besides, the burden imposed on the consumers under the quota regime is more disguised and imperceptible to the general public than the incidence of import duties No wonder, therefore, if the executive has imposed quota restrictions more frequently and with dangerous consequences on the volume of world trade

The import quota system has led to unlimited discrimination in modern commercial policy Being arbitrary and rigid, the import quotas ipso facto spell unfair discrimination Further, since the Most-Favoured-Nation Clause could not be applied to them, the scope for discrimination has increased considerably The spirit of the Most-Favoured-Nation Clause in the commercial treaties though probably not its letter is violated The principle of equaliy of treatment which is essential for the development of world trade, has ceased to operate Discrimination, retaliation and trade wars have become a familiar feature of modern commercial policy

The administration of the import quota system is complicated and implies continuous government interference into business affairs In the allotment of quotas there is a wide scope for favouritism between different countries and importers In fact, discrimination is inherent in the import quota system If international trade is to develop on normal lines, the import quotas and other abnormal restrictions on trade must be removed

CHAPTER V

EXCHANGE CONTROL

MONETARY policy has proved an invaluable instrument of promoting foreign trade No wonder, therefore, that few economic questions have received so much attention since the setting in of the depression as monetary policy. In the domain of foreign economic policy, the main object of a country's monetary system is to secure relative stability of exchanges, with a view to maximising foreign trade, consistent with a reasonable internal economic stability. Reference has been made in the second chapter to the dislocations caused in the internal economic structure by the world depression Recent changes in the national monetary policies are, therefore, instructive because they show how individual countries have tried to mould their monetary policy to protect their economic systems from the ravages of the depression and repair the damage caused thereby Of these changes, the system of exchange control is significant

In its widest import, exchange control means the interference, no matter what form it assumes on the part of the monetary authorities in order to control exchange rates [1] Thus construed, exchange control is a *sine qua non* of a stable monetary system, without it no international monetary system could exist Therefore one of the essential duties of a central bank is to eliminate unhealthy fluctuations in exchange rates and maintain thereby the external stability of the national currency An unregulated monetary system would lead to arbitrary fluctuations

in the relative values of different currencies and upset the normal movements of capital and commerce

Indirect or Normal Form of Exchange Control.—The pre war currency system whether the gold standard or the gold exchange standard was based on a conscious regula tion of exchange rates by the central banks The gold standard was not absolutely automatic even in Great Britain and still less in other countries It was the duty of central banks to intervene from time to time in order to safeguard the stability of the currency [1] The fluctua tions of exchanges were regulated through the purchase and sale of gold at fixed prices in the case of gold standard and the purchase and sale of gold exchanges in the case of gold exchange standard In addition the bank rate was manipulated to minimise the flutuations Similarly open market policy was used to control exchange rates by regulating the rate of interest Above all the foreign exchange during the export season and its sale during the import season was the most important instrument of exchange control In short the credit policy was frequently manipulated to keep the foreign exchange rates within the gold points.

Direct Form of Exchange Control.—The aforesaid devices constitute an indirect or normal form of exchange control With the new developments in the technique of commercial policy during the depression these forms of exchange control have faded into insignificance and instead we have more aggressive types in the forefront These measures regulate the demand and supply of foreign exchange directly The present chapter will therefore be concerned primarily with these direct measures

Objective of Exchange Control—The world economic crisis has created new problems more complex in their character requiring a radical cure Due to political

1 Vide Einzig "Exchange Control," p 19

"Even the pre-war gold standard meant a conscious regulation by Central banks" says Prof Bertil Ohlin. The American Economic Review March, 1937

psychological and economic causes the flow of abnormal liquid balances from one centre to another has become more frequent and cannot be offset by the automatic working of the exchanges Experience has shown that the effects of these movements on national currency can be neutralised promptly and effectively only by direct action, the indirect methods would hardly produce the desired effects under modern conditions which have changed considerably as compared with those before the war or even those of the pre-depression period This direct action would consist of purchasing the exchange sold when these funds flow in, and to keep the exchange ready for re-sell when these funds flow out In the absence of such direct action, the inflow of funds will cause an unhealthy appreciation of the exchange, disturbing thereby the entire economic structure Besides, the central bank, having failed to accumulate foreign exchange, is in such a case faced with a choice between satisfying the demand for foreign exchange out of its own reserves or allowing the national exchange to depreciate under the pressure of the withdrawal of funds, with disastrous consequences Under these circumstances, the acquisition of an equivalent of the inflow of foreign funds is not a luxury, but a necessity [1]

Another important objective with which direct exchange control measures have been applied is to regulate the fluctuations in trade balances The classical rule, that an adverse trade balance automatically corrects itself if allowed to bring about a depreciation of exchange, does not hold good under modern conditions marked by excessive trade barriers The operation of normal correctives is apt to be delayed, and the sufferings during the period of transition intensified The adverse balance of trade has therefore, to be corrected immediately with the application of direct measures in the form of import restrictions and bilateral balancing of trade [2]

Exchange control is also used to guard against the dangerous consequences of the flight of national capital. In these cases the regulations can be enforced more effectively and efficiently because of the presence of the owners of capital within the national boundary and their stake in the country. This flight may be either to or from the national currency.

Similarly, the speculative influence upon exchange rates must be controlled in order to permit the level of exchanges being determined by economic forces. In practice however, it is difficult to separate the genuine economic forces from pure speculative ones. The State, therefore, has to undertake the onerous task of determining the economic parity of exchange and of maintaining it at that level with the aid of exchange control measures. Those entrusted with this highly complicated and technical task are apt to commit mistakes, either by bolstering up the exchange artificially at an untenable level or by keeping it at an unduly low level, which would prolong and aggravate the crisis. But the scope for error can be minimised if the authorities are kept well informed and the policy is carefully planned and continuously pursued.

Another important feature of the commercial policy since the depression is the common and extended use of exchange control. As a result of this even those countries which would not be normally willing to use exchange control measures are drawn into the net due to close international economic interdependence. They have perforce to apply these measures in self-defence, in order to neutralise the adverse effects of exchange restrictions imposed by other countries. Thus the contagion spreads.

Technique of Exchange Control.—The exchange rates may be regulated in two different ways. The first method consists in the monetary authorities undertaking to purchase and sell foreign exchange, in order to regulate the rates, leaving at the same time the right of private citizens to buy and sell exchange unrestricted. Here the

monetary authorities vary gold or foreign exchange reserves of the central banks or the exchange equalisation funds to realise their objective This may be called the British method Under the second method however, the freedom of market is destroyed completely the supply of foreign exchange is brought under the direct control of the State, and the private citizens are permitted to purchase it subject to the conditions imposed by the State authorities The distribution of foreign exchange is rationed This form of control has been developed by Germany The second method is certainly more strict and seems to have been dictated by Germany's acute exchange difficulties Germany could not probably attain its objective otherwise It is said that free dealings in exchange would have risked German economy

The Moderate Type of Exchange Control—We shall now proceed to analyse the moderate form of exchange control exchange stabilisation funds This system has developed since the breakdown of the international gold standard and represents an important departure from traditional methods In this connection the organisation and working of the British Exchange Equalisation Account would make an instructive study in methodology

The Post War British Gold Standard—At the time of the restoration of the gold standard in England in 1925 the pound was over valued by about 10 per cent It was expected that a rise in prices abroad would bring about the desired adjustment but instead the downward trend of prices widened the disparity and increased the difficulties of the British industries and commerce The British gold costs remained inflexible and unadjusted [1] Under these circumstances it was expected that the British industries would gradually reduce their costs of production by increased efficiency but the depression set in before the equilibrium was restored and added to the difficulties Notwithstanding severe strain on the British trade and industries the Balfour Committee in 1929 held that it

was unthinkable to favour a fresh departure from the gold standard. Even as late as June 1931 the Macmillan Committee recommended that England should continue to adhere to the international gold standard

Difficulties leading to the Suspension of Gold Standard In 1931, the British balance of payments became heavily unfavourable, because whereas the exports recorded a serious setback and the income from investments, shipping and financial services dwindled the imports continued to pour in their full strength The situation was serious Sterling was subject to severe strain A country's power to maintain exchange stability and its capacity to borrow or lend abroad depend upon the balance of its international payments and upon its credit British credit was also shaken, because British short-term foreign loans became frozen and foreign funds were withdrawn The result was a run on the pound during the summer of 1931, and in about two months' time more than £200 million were withdrawn from London The drain continued and the attempts to support sterling by borrowing proved fruitless[1] The gold standard had, therefore, to be suspended in September, 1931

Effects of the Suspension.—The immediate effect of the suspension of gold standard was a fall in the value of the pound The depreciation of sterling stimulated British exports,[2] and checked imports The protectionist policy adopted by Britain further helped to restrict imports and encouraged British trade and industries The adverse balance of payments was soon corrected and confidence in sterling restored[3] As a matter of fact, early in 1932 it seemed that the pound would rise externally, before the international system had had time to adjust itself to the new level of exchanges[4]

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1 In order to support sterling the Bank of England borrowed £50 million and the Government £ 80 million on short term from Paris and New York

2. The expansion would have been much more marked but for the growing trade barriers.

3. Confidence was restored with the prompt repayment of the amounts borrowed from Paris and New York.

4 Vide Hall, N F "The Exchange Equalisation Account" p 3

Thus, in 1932 the pound had to be pegged against upward movements At this juncture, the authorities did not intend to resort to "deliberate under-valuation". What they wanted was "to prevent changes in foreign balances moving the exchange away from the equilibrium rate at which it was tending to settle under he influence of normal long-term industrial factors"[1] The abnormal factors, calculated to upset the economic equilibrium alone had to be regulated The sad experiences of the sudden movements of short-term capital on large scale were too fresh to be neglected[2] These movements were often speculative and increased monetary and financial instability To eliminate this speculative and uncertain element it was thought desirable to have a separate exchange stabilisation fund Accordingly, the Exchange Equilisation Account was set up in April, 1932 It is a sub-department of the Treasury[3]

The Exchange Equalisation Account—The fund was intended, as aforesaid, to prevent the foreign balances from dislocating the exchange equilibrium, the movements of foreign balances had to be carefully watched and their undesirable effects neutralised London had become an important centre for the temporary accumulation of large short-term balances and adequate liquid funds had to be provided, in the case of sudden and untimely withdrawal of these balances on a large scale, to protect the internal economic structure The principal function of the Exchange Equalisation Account, therefore, is to build up sufficient liquid resources to be able to meet these contingencies,

in order to prevent the short-term capital movements either disturbing the external value of the pound or internal short-term money rates It is essential to remember that the Exchange Equalisation Account is not intended to interfere with long term trends, the fundamental criterion is to eliminate temporary fluctuation in the rates caused by the speculative influx or efflux of bad money', without interfering with the long term trend of the market Any change in the fundamental position is to be given full freedom to work itself out The exchange rate of the pound must reflect the internal cost and price structure That is, if Britain is faced with an adverse balance of trade after making allowance for normal capital movement, due to higher cost and price structure in Britain, the Account will not interfere and allow the foreign exchange value to decline The same policy of non interference will be followed if the foreign exchange value of the pound rises due to favourable balance of trade resulting from lower cost and price level in Britain.

The Practice of "Offsetting"—To achieve this objective, the practice of "offsetting" has been followed, which prevents the short term capital movements from affecting the cash basis of the domestic credit structure [1] In the case of an influx of foreign balances the authorities try to meet the situation by selling Treasury Bills in the money market, which are largely purchased by the commercial banks The receipts of the Treasury Bills are utilised for acquiring the foreign balances in the exchange market These are almost immediately converted into gold. The practice is in favour of gold holding [2] In some cases the incoming foreign balances are invested by their holders directly in Treasury Bills The result of this new mechanism is in the case of inflow of foreign balances to increase the Treasury Bill holdings and deposit liabilities of the commercial banks,

1 Vide Monetary Review (League of Nations) 1936-37 p 52.

2 "The Account naturally does not want to put itself in the position of a speculator in foreign currencies and accordingly it makes a practice it is understood, of exchanging foreign currencies acquired for gold almost immediately If it did hold foreign currencies for long the system would be analogous to a gold-exchange system and might have slightly different repercussions from those discussed in the following paragraph. But as the practice appears to be definitely in favour of holding gold and not foreign currencies we shall assume that gold alone is held." Vide Sayers, R. S.: "Modern Banking," pp. 197 98

their cash reserves are unaffected In the case of an outflow of these foreign balances, the Exchange Equalisation Account sells gold and with the proceeds of these sales repurchases its Treasury Bills In this case, again, the Treasury Bills and the deposits of the banks decline and the cash held is unaffected

Here, however, it is interesting to note that the domestic credit structure is not entirely immune from the effects of the movements of foreign funds Doubtless the absolute quantum of bankers' cash reserves remains unchanged But, in the case of an inflow of foreign balances the volume of bank's deposits increases and their cash ratio is lowered [1] which is apt to raise the money rates Similarly, in the case of an outflow of foreign balances the deposits are diminished, and the cash held by the banks remaining the same, the ratio of cash to deposits is raised and the money rates tend to decline The authorities realised these repercussions, and a part of gold was transferred from the Exchange Equalisation Account to the Bank of England, to help the commercial banks to support the larger volume of deposits resulting from an inflow of foreign balances without an undue reduction in their cash ratio When the commercial banks show signs of contracting credit due to fall in the cash ratio the central bank should restore the cash ratio by purchase of securities Thus the Exchange Equalisation Fund used the "offsetting" mechanism to provide a cent per cent cover for the foreign short-term funds invested in London to prevent a repetition of the difficulties experienced in 1931 in connection with the effects of sudden foreign withdrawals on a large scale on the internal credit supply and the external exchanges [2] The mechanism is similar to the open market operations resorted by the

central banks under the gold standard to offset the movements of gold, there is nothing particularly new or original about it It has merely improved the old devices and increased their effectiveness Under a sound banking system, the character and magnitude of deposits determines the size of the cash reserve held against them

Elasticity of the Mechanism—The elasticity, which is the characteristic feature of the Exchange Equalisation Account has put invaluable check upon speculation, with minimum disturbance to the internal credit structure [1] Within the maximum limit laid down by the Parliament, for the issue of Treasury Bills, the authorities had full power to check the speculative tendencies to bull sterling Again, this maximum could itself be changed with the approval of the Parliament, as was done in the Budget of 1933 But it needs to be noted that the maximum limit prescribed indicated the extent to which the authorities would be prepared to go to regulate the undesirable disturbances to sterling It does not imply that the Account operated to its full capacity The mere threat was often sufficient to check the speculators, and prevented the external rise of the pound

Self-liquidating Character—Further, the Exchange Equalisation Account effects an automatic adjustment of foreign exchanges The extent or magnitude of the foreign reserves vary in conformity with the variations in foreign balances With the increase in foreign balances an equal amount of foreign exchanges is purchased and the adjustments between the supply of Treasury Bills and the holdings of foreign exchange are perfectly automatic and self-liquidating The internal credit structure is undisturbed

No Fixed Rate of Stabilisation—Thus the new mechanism of *"offsetting" regulates the foreign balances* so that they may help, rather than embarrass the money market [2]

1 "The secrecy with which its dealings have been surrounded and the absence of any declared principles of action has made it extremely difficult for speculators in exchange to interfere" Vide Prof Ohlin's "The American Economic Review" March 1937

2. Vide Hall N F's "The Exchange Equalisation Account" p 32

It has facilitated the movements of short term capital and used them for improving the external reserves And this was effected with minimum risks The reason is that the persons controlling the Exchange Equalisation Account are authorised to fix at their discretion the prices at which they would purchase foreign exchange and gold which eliminates the rigidity and the waste inherent in a fixed rate [1] This new device is therefore very efficient and economic

Interdependence Between Gold and Note Issue Weakened Another instructive feature of this new mechanism is the weakening of the direct interdependence between the gold held by the Bank of England and its note issue Gold is held primarily against external liabilities, it does not directly regulate the internal credit structure The acquisition of gold and foreign exchange does not cause a corresponding increase in the British credit structure This change has been effected because 'London is now practising international deposit banking as distinct from international acceptance business' [2]

International Acceptance Business—The international acceptance business tends to be self liquidating in character [3] The British houses accept and float foreign bills in the London money market and the time of maturity in different cases is properly arranged so that the continuous buying and selling of sterling tends to favour the pound In addition the bank rate corrects in time the disturbances resulting from the changes in the volume of business

International Deposit Banking—In the case of deposit banking however the conditions are entirely different The timings of different transactions are unplanned and uncertain particularly when the movements of these funds are determined more by the political and psychological factors than strictly economic The adjustment between the purchase and sale of sterling therefore becomes diffi-

cult. To meet this difficulty it is essential that the authorities should acquire gold and foreign exchange in proportion to the inflow of foreign balances Further, if the inflow of foreign funds is due to the relatively high level of money rates in the domestic market, the fresh gold acquired should be utilised to lower the money rates and increase the credit structure, so as to effect an equilibrium between the domestic and foreign costs and prices Here, the orthodox gold standard practice would re-establish the desired equilibrium But when the inflow of foreign balances is due to political and psychological causes, as has been the case since the depression the normal gold standard procedure would add to the difficulties, instead of removing them It would deplete the resources of the suspected currency systems, enlarge the credit structure and weaken the balance of payments Therefore, the practice of "offsetting" has been adopted and the disturbances minimised "It appears, therefore, that so long as London practices international deposit banking instead of acceptance business, a policy of 'offsetting' similar to that carried on by the Exchange Equalisation Account will be necessary as a normal feature of British monetary policy"[1]

The Exchange Equalisation Account has been invaluable in maintaining exchange equilibrium[2] It is interesting to note that during the years when foreign balances were accumulating on a huge scale in London the Exchange Equalisation Account continuously purchased gold and prevented thereby a rapid rise in the exchange value of sterling When the movement of foreign balances was reversed and sterling sold on a huge scale, the Exchange Equalisation Account sold gold readily and helped to maintain a fairly steady exchange rate for sterling Thus, the internal economic structure is kept fairly immune from the large and irregular movements of foreign funds External influences can no longer cause a serious disturbance to internal

1 Vide Hall "*The Exchange Equalisation Account*," pp 90-91

2 "It is true that the Exchange Account system has represented technical improvements as compared with the pre-war devices for insulating the circulation needs from international gold movements and of course represents far greater improvement over the very unsatisfactory systems of 1925-31" Vide Sayers R S "Modern Banking" p 209

credit Under the gold standard, however, with the statutory obligation to maintain the pound sterling at a fixed gold value, the money market was extremely vulnerable to external influences 'Today the Bank of England is no longer under this obligation, there is freedom to allow the rate of exchange to swing more widely and by judicious purchases or sales of gold as foreign balances increase or diminish, to take the weight of great international movements of funds without affecting internal trade credit"[1]

The Netherlands Stabilisation Fund—The principle of "offsetting" was also incorporated in the stabilisation fund set up in the Netherlands on the 30th September, 1936, for preventing excessive fluctuations of the florin The Fund was allotted 300 million gulden in Treasury bills, one-third of which it immediately exchanged for gold at the Netherlands Bank in order to provide against the contingency of an outflow of capital and an undue depreciation of the currency Thereafter the movement of capital proved to be definitely *inward* and the Fund *offset this inflow by selling* Treasury Bills and converted the receipts into gold The Treasury Bills held by the Fund were soon exhausted and its maximum capacity being limited to 300 million gulden it transferred large stocks of gold to the Netherlands Bank[2] The acquisition of gold by the Bank could not fail to expand the cash basis of the internal credit structure The offsetting capacity of the Fund ought to have been enlarged to meet this contingency

January 31, 1934, "for the purpose of stabilising the exchange value of the dollar,"[1] followed a different method. The structure of the American Fund was different It was composed, not of assets in domestic currency, but of gold, amounting to $2,000 million Of this sum, $200 million formed the working capital and the rest was kept intact in its original gold form The continuous inflow of gold was absorbed by the funds obtained from the Federal Reserve Banks in exchange for gold certificates equivalent in amount to the gold acquired. The result was an expansion of the credit base There was a short-lived outflow of funds in 1935, and this had to be met by the sale of gold The resources of the Fund declined by $200 million and led to the contraction of domestic credit But it may be said that the huge inflow of foreign funds was only partially absorbed in the domestic credit structure, the rest led to the excessive growth of cash reserves with the American banking system. The minimum reserve requirements were successively increased in order to prevent excessive credit expansion and immobilise the bulk of the excess reserves as a cover for the foreign balances This provides the assurance that the repatriation of foreign funds can be effected with a minimum of disturbance to the United States This policy has been supplemented by another device Since December 1936 the United States Treasury has followed the policy of "sterilisation" of gold, under which the gold purchases are financed, not by the delivery of gold certificates to the Federal Reserve Banks but, by the issue of additional short-term treasury obligations, on

1 According to the Secretary of the Treasury the Stabilisation fund is normally concerned with hour-to-hour and day to-day fluctuations in the dollar exchange rate Sometimes it is called upon to *prevent violent fluctuations in exchange rates induced by acute political* developments which cause flights of capital from one country to another When the exchange rate between the dollar and the currency of a country with small gold holdings is subjected to pressure because of unfavourable political or economic developments the fund can be employed, and has occasionally been employed in such circumstances to help stabilise the dollar exchange A further use of the fund has been to assume in times of stress in the foreign exchange market the functions normally performed by private operators who because of the risk involved may not be willing to act at the very time when there is the greatest *need for exchange facilities In fact on several occasions the fund was virtually the only* source of dollar exchange As regards the future when with the restoration of normal economic conditions in the world gold may leave the United States in large volume the gold in the Stabilisation Fund will cushion what might otherwise constitute a severe shock to the American economy

the money market[1] This is the American practice of "offsetting"[2]

The French Exchange Stabilisation Fund—The French Stabilisation Fund was set up in October, 1936, with 10 milliard francs in gold The object of the fund was 'the regulation of the relation between the franc and the foreign currencies, while maintaining the parity of the franc in relation to gold within the limits fixed' by the statute The fund was placed under the management of the Bank of France, but it was to be worked on account of and under the responsibility of the Treasury The working capital of the fund was provided from the revaluation profits The assets of the Fund did not consist of national currency which could be sold on the domestic market to meet the inflow of foreign balances The result was that in the case of import of foreign capital the Fund had perforce to pass on the gold acquired by them to the Central Bank In this case however, due to certain political and economic causes there was a continuous outflow of funds from France and the gold holdings of the French Stabilisation Fund were exhausted by June 1937 The return flow of funds which took place in the last quarter of 1937 brought about 10 milliard francs of capital back to France But inflow of funds stopped in December 1937 and the beginning of 1938 saw a recrudescence of capital flight due to political factor both internal and external The Exchange Stabilisation Fund lost large amount of gold in attempting to check the fall in the gold value of the French franc The new French

Government allowed the value of the French franc to fall by 10 per cent, in addition to 10 per cent fall which had already occurred due to flight of capital, but declared that no further fall in future would be allowed This led to repatriation of capital on a large scale, which the resources of the Exchange Stabilisation Fund could not absorb The supply of francs at the disposal of the Fund had therefore to be enlarged

The Swiss Exchange Stabilisation Fund—The Swiss Stabilisation Fund, set up on 30th September 1936, adopted a similar practice The Fund has been used to maintain the value of the Swiss franc in terms of gold It started with the capital of 539 million Swiss francs in gold There were no treasury bills or other assets in national currency the Fund could sell to offset the import of foreign capital. It had to hand over the newly acquired gold to the Central Bank No wonder therefore that the gold reserve of the Swiss National Bank gradually increased

From the foregoing review it will be seen that the exchange equalisation funds are of two types, those whose initial resources consist of assets convertible into domestic currency in the open market and those whose initial resources consist of gold The funds of the former type are capable of neutralising the effects of floating balances on the internal credit structure The structure of the funds of the second type does not allow them to offset the movement of short-term capital Faced with an inflow of gold, they are, in themselves, powerless to prevent an expansion of internal credit Similarly, in the case of an outflow of capital, they are unable to prevent a contraction of credit This contraction can be prevented if the Central Bank balances thus acquired are reinvested in the open market [1]

The Rationing Method of Exchange Control.—This type of exchange control restricts the liberty of private indivi-

1 Vide, "Monetary Review" (League of Nations), 1936-37 p 58

duals to deal in foreign exchanges[1] Under the system several devices are used to keep the external value of the national currency higher, by proper regulation and control, than it would otherwise be In some cases attempts have been made to keep up the original par value of the currency. Germany is an interesting example of this type. Another device is to use exchange control, after an initial depreciation, in order to prevent further depreciation. The Danish currency has been rationed so as to keep it at a fixed ratio with the pound sterling The third type of rationing control is used to obtain the supply of foreign exchange for the payment of foreign debts at costs lower than would otherwise be possible The South American countries have used this device[2]

The exchange control attempts to regulate speculation, as stated above It is admitted that speculative fluctuations in currency systems are not desirable, because these disturbances damage the economic structure of the State Therefore to the extent to which the exchange control curbs the speculative tendencies, it permits, rather than prevents, the normal functioning of the economic system. It may be said that exchange control of the moderate type, described above, has been very successful in controlling speculation. One is therefore led to doubt the desirability of resorting to the rationing type of exchange control for achieving this objective, which has been adequately achieved by the more moderate methods.[3]

It has also been noted that huge international capital movements, characteristic of the depression period, constitute a very powerful disturbing force to the smooth functioning of the economic system These movements are

partly due to economic and partly to political and psychological causes In this sphere, too, the exchange control of the moderate type has a creditable record. It has tried to isolate the movements due to economic and non-economic causes and the technique of the correctives applied has been suitably modified to suit the conditions For instance, where the movements are the result of some genuine disequilibrium between the domestic and foreign costs, which shows itself in a relatively high level of money rates in the local market, the Central Bank, on the entry of foreign funds, acquires gold, uses the same for increasing the credit structure, lowers money rates and helps thereby to raise the domestic cost and price structure in conformity with the normal gold standard procedure The lowering of money rates in the domestic market checks the influx of foreign balances This is not all Soon after the equilibrium between the domestic and foreign costs is established, the foreign deposits will gradually flow out, without disturbing the internal economic structure The practice of "offsetting," described above, tries to neutralise the effects of the movements of foreign balances, on the internal credit structure, due to causes other than the disequilibrium between the internal and external cost and price structures In the case of the rationing type of exchange control, however, the restrictions are applied indiscriminately against every kind of capital movements which often add to the disturbances they attempt to resrict and cause irreparable damage to the economic system

The use of the rationing type of exchange control, to maintain the original par value of the currency, has sometimes been defended on the plea that it helps to restrict the increase in the external debt burden. German government has often advanced this argument It is difficult to appreciate the efficacy of this expedient The defence of the old par has hardly helped to reduce the real burden of debt payments for the German people In view of the depreciation of the pound and the dollar, in which currencies most of the German foreign debt was contracted the German

mark could have availed of the proportionate depreciation without any increase in the debt Besides since the foreign debt payments are made by means of an export surplus of commodities Germany, by keeping the mark at its old par, cannot charge for her commodities prices higher than those she could have done under a proportionate depreciation of her currency The German attempts to maintain the old par value of their currency would have adversely affected their trade and industries New methods were devised by Germany and other countries to counter the economic difficulties These new methods implied a more strict control and rationing of foreign exchange To understand in full the economic implications of these new devices it is essential to examine the structure of rationing type of exchange control in greater details with special reference to modern Germany

Economic Conditions in Germany—The tendency towards a slump which was discernible in 1929 became much more pronounced in 1930 There was a world wide fall in gold prices especially of foodstuffs and raw materials which was accompanied by a universal contraction of industrial production and of money incomes The economic consequences of the setting in of the depression became more serious for Germany due to decrease in the imports of foreign capital which practically ceased in the second half of 1930 With the cessation of foreign credits the internal market both for imports and for domestic goods contracted and the reparation payments together with accumulated interest had to be met largely out of taxation Further it led to a continued rise in real wages and increased the cost of the maintenance of the growing number of unemployed The burden of taxation therefore increased The economic conditions of German agriculture had also materially deteriorated [1] The Reichstag elections in September 1930 which recorded large gains both to the National

Socialist and the Communist parties, shook internal confidence and led to a flight of German capital abroad.[1] In March 1931 the French bitterly opposed the proposal for a customs union between Germany and Austria and withdrew considerable sums from Germany in order to exert political pressure. These developments shook belief in the efforts made to secure economic stability in the post-war Europe.

The collapse in May 1931, of the most important Austrian bank, the Credit Anstalt, gave a rude shock to those who believed in the success of post-war economic policy and the stability of the economic structure of the world. Germany suffered most from this catastrophe. There was a flight of capital on large scale from Germany. Foreign creditors began to recall their German funds on a large scale. The magnitude of the funds withdrawn was so great that the Reichsbank was forced to withdraw its support of the very important Darmastadter and National (Danat) Bank, which was compelled to close its doors on July 12, 1931. The failure of this bank led to a general run on all the banks and savings banks, and the Government had to close all banks and other credit institutions on July 14, 1931. They were re-opened on August 5, subject to a Reichsbank discount rate of 15 per cent.

In view of the foregoing difficulties, all foreign exchange dealings were centralised with the Reichsbank on July 15, 1931, and later foreign exchanges were brought under official control.[2] This was not enough. To meet the problem of foreign debts the German Government had to enter into standstill agreements. These agreements provide for 'acceptance credits' and cash advances. First standstill agreement was entered into with foreign creditor banks, on September 1, 1931, to remain in force till March 1932, for restricting the withdrawal of short-term commercial and

1. The Reichsbank lost 700 million RM. in gold and foreign exchange holdings. The loss would have been much greater but it was checked due to a rise in the Reichsbank's discount rate to 5 p.c. and a special temporary credit of £35 millions from America.

2. Great Britain has also centralised foreign exchange dealings since November 1939 and placed them under strict official control.

financial credits amounting to 6 milliard R M Under the Agreement, German banks were required to obtain from their clients either valid acceptances or promissory notes to be held in trust as a collateral security for the foreign creditors Further, the German banks were required to devote the payments made by their clients in respect of these bills to buy foreign exchange for remittances to foreign creditors against outstanding acceptances If the requisite foreign exchange could not be supplied, payment had to be made to the Reichsbank into the account for the foreign creditor who should be entitled to dispose of his balance as best as he could after three months The German debtors were also required to cover all acceptances on maturity with either cash or "replacement" bills, which could be rediscounted by the creditors in their countries The Gold Discount Bank undertook to remit the payments on acceptances in three equal annual instalments The foreign creditors agreed to maintain their advances, but they were given the right to arrange with their debtors for the repayment of credits due, on condition that they held a similar amount in credit facilities at the future disposal of the debtors

The abandonment in September, 1931, of the gold standard by England and a number of other countries and a great extension of foreign exchange control, quotas, and import restrictions throughout the world put a very severe strain on the German economic system To meet the new situation Dr Bruning's Government accelerated the process of deflation The immediate effects of this policy were to accentuate the depression Steep fall in prices, wages and profits with rising unemployment,[1] led to a material diminution in the total money income and in the effective demand for both imports and domestic output Every contraction in income led to a further contraction of employment So far as industrial structure is concerned, the

greatest volume of contraction was experienced in the investment goods industries Disinvestment was taking place in working capital, the volume of replacements diminished. As regards German agriculture, full force of the contraction of incomes and purchasing power of the people was felt by the German farmers The decline in agricultural incomes, in its turn, contributed to contract the market for industrial goods The state of public finances was much more serious The volume of public indebtedness had increased enormously, and the public bodies were crippled by the interest payments they had to make Further, the decline in output, together with the liquidity of the banks following the crisis of July, 1931, restricted severely both the supply of and demand for credit Private savings had almost disappeared

To alliviate the situation so far as foreign creditors were concerned, second Standstill Agreement was entered into in February, 1932 The creditors agreed to maintain their short-term credits for another year The credit base was extended and arrangements for the progressive repayment of 'unavailed' portions of the outstanding credits were made A partial consolidation of unsecured advances was provided for Creditors of certain funds were given the option of investing their funds in Germany The creditors were entitled to an initial 10 per cent permanent reduction of the outstanding credits The creditors who found the unavailed portion of the credits placed at the disposal of their debtors insufficient to effect the aforesaid 10 per cent initial reduction were to be given a preferential right or repayment at the subsequent reductions until this initial deficiency had been made up This provision introduced an element of discrimination Further, a trust fund was created at the Reichsbank into which German bank-debtors were to pay assets equal to 5 per cent of the unsecured cash advances and the Reichsbank was to issue collateral trust certificates against those unsecured advances The creditors were also given the right to convert unsecured advances into Reichsmarks for long-term invest-

ment in mortgages, real estate, securities, etc These provisions gave a definite mould to the system of 'blocked marks' to be discussed in the subsequent section

As regards the internal recovery, Dr Bruning's deflationary policy did not succeed in improving the situation The Von Papen Government, which replaced Dr Bruning's, formulated a definite policy to stimulate investment and increase employment The issue of tax certificates and a programme of public works were the most important features of this policy The Papen Government was, however, short-lived The National Socialist regime[1] under Herr Hitler, which came into power on January 30, 1933, adopted a more definite policy and a vigorous drive to cure unemployment The National Socialists, on coming into office, took over a number of measures which were adopted by Bruning and Papen Governments to cure unemployment, perfected them and applied them on a more extensive scale[2] with a firm determination and will to improve the economic structure of Germany and its military might. The rationing type of exchange control was an important feature of this policy

Purposes of Rationing Method of Foreign Exchange Control—Foreign exchange regulations differ considerably from country to country according to the economic conditions of the countries resorting to them and the objectives they were intended to achieve These difficulties were partly financial due to the withdrawal of capital excessive burden of foreign debts and the shortage of foreign exchange, they were partly psychological due to the lack of confidence in the currency both at home and abroad, fear of devaluation and hyper-inflation or the fear of an absolute collapse of the banking and financial structure of the

country, and, the difficulties were partly economic, due to diminution of the export markets, the collapse of prices, the imposition of quotas and other trade restrictions abroad, leading to an adverse balance of payments and a general economic disequilibrium. The more important reasons for introducing exchange control may therefore, be briefly noted.

1 **To Stabilise the Exchange Rates** —A number of countries introduced exchanged control in order to prevent depreciation of their currencies when they found that the original exchange rates could not be maintained. To this group belong Germany Hungary Czechoslovakia, etc These countries introduced exchange restrictions in order to maintain fixed and arbitrary rates of exchange at any cost This was a faulty policy to adopt As a result of this faulty policy economic difficulties of these countries increased. Therefore the basis of exchange restrictions was widened and they were enforced more strictly and rigidly The methods of supervision and allocation were very carefully thought out and scrupulously enforced

2. **To Conserve the Gold Supply.**—With the setting in of the depression pressure on the gold resources of certain countries debtor countries in particular had increased. This meant that if gold standard was to be maintained, a fall in gold stocks would lead to deflation and unemployment Abandonment of the gold standard they thought would lead to hyper inflation, for which they were not prepared. This strain on gold resources of the debtor countries was due largely to the faulty policy adopted by the creditor countries who almost declined to receive payments in goods. To prevent deflation of their gold resources and a consequent collapse of their economic system, the debtor countries were compelled, in self-defence, to resort to exchange restrictions

3 **To Prevent the Flight of Capital.**—The flight of capital on a large scale, distinct from normal movements of capital due to higher rates of interest presents a very serious pro-

blem, because it causes a serious setback in the economic activity of the country affected All classes of people are adversely affected and the financial structure is threatened with a collapse The measures that may be taken to prevent the catastrophe must necessarily be prompt and effective Exchange restrictions are, therefore, introduced to check the flight of capital The nature and extent of the exchange restrictions differ according to the intensity of the flight and the causes responsible for it For instance, if the flight of capital is due purely to speculation, it can be checked with relatively simple restrictions Similarly, if the flight is due to temporary disequilibria in the economic structure of the country, it may be checked by suitable regulations reinforced by a proper economic policy calculated to restore the required equilibrium If, however, the causes are more deep-rooted, the remedy, to be effective, must also be more radical and strong, the restrictions must be rigid and stringent

It is necessary to note that exchange restriction, to be successful in checking the flight of capital and runs on deposits, in countries where people had lost confidence, had to be supplemented by an effective regulation of commodity trade To make the restrictions more effective and prevent evasion both financial and commercial transactions had to be controlled Therefore, exchange restrictions have been invariably extended to cover commodity trade

4 **To Assure Essential Imports** —The countries which were faced with the shortage of foreign exchange could not permit free imports They had to discriminate between imports to make the most effective use of limited foreign exchange they possessed Further, due to the policy of economic self-sufficiency adopted by most of the advanced countries, imports were being regulated generally The fear of war was also responsible for producing all essential products within national boundaries and securing an adequate supply of those which could not be produced Imports, therefore,

were broadly sub-divided into essentials and non-essentials Exchange restrictions were introduced to secure an adequate supply of essential imports If there was surplus of exchange it could be used for non-essential imports Strict rationing of foreign exchange was resorted to and all importers had to obtain an official permit. For instance, in Germany, before Dr Schacht took charge of the Ministry of Economics in July 1934, importers were given foreign exchange allotment in proportion to the amount they had imported before 1931 This allotment was gradually reduced due to financial and exchange difficulties In February 1934 the allotment was 50 per cent, but by May it had fallen to 5 per cent., and later day-to-day allotments were made, based on the Reichsbank's intake of foreign exchange In September 1934 Dr Schacht announced the so-called New Plan for foreign trade Under the new arrangements the former system of foreign exchange allotment by quotas was replaced by a system under which a foreign exchange certificate had to be obtained for every individual transaction before a definite order could be placed and goods imported.[1] Other devices were used later, which we shall discuss presently

It is essential to note at this stage that though one of the objects of exchange control has been to improve the balance of merchandise trade by restricting imports, in practice, the exchange restrictions have had adverse effects on the export trade In the first place, exchange restrictions created a wide disparity between the internal and external price structures, the internal price levels of the countries rationing foreign exchange were much above the world price level. This was due to the policy of credit expansion adopted by them. As a result of the relatively higher internal price structure the export ability has been adversely affected. Goods exported by the countries resorting to exchange control became dearer, due to the over-

1 The administration of the Plan was carried out by twenty-seven Control Boards, based on the industries or raw materials concerned. These Boards were responsible for giving exchange certificates and for deciding for which countries and for which goods the available supplies of foreign exchange should be used. Vide, Guillebaud, C. W., "Economic Recovery of Germany pp.67-68.

valued internal currency and relatively high prices in terms of domestic currency Besides, due to exchange restrictions export trade becomes unattractive Hence export subsidies on a large scale were offered to stimulate the exports Notwithstanding these encouragements export trade of exchange control countries has gradually declined and increased the adverse balance of trade Thus, exchange control has tended to increase the defect it was intended to remove

5 To Provide Exchange for Meeting External Debts of the Government—Certain governments had huge debts to be paid Germany was the most important country belonging to this group The German Government had a huge burden of reparations Further the German Government financed reparations out of foreign loans This policy concealed from the creditor countries the real economic position of Germany and its ability to pay reparations and the problem of transfer Under normal circumstances Germany, given the ability to pay the reparations would have been able to pay only if she was allowed sufficient export surplus and the creditor countries accepted a sufficient import surplus Germany introduced exchange restrictions partly to meet these claims She entered into standstill agreements in the earlier stages In June 1934 however transfer of interest by foreign exchange payments was completely stopped in principle and foreign creditors were offered ten year Funding Bonds bearing interest at 3 per cent This led to the negotiation of Payments Agreements In addition an extensive system of private compensation agreements grew up

6 To Serve as a Bargaining Instrument—Exchange restrictions have been used to bargain for concessions or to secure a relaxation in the rigidity of the rationing of foreign exchange The authorities have used exchange control to discriminate between different countries in respect of the imports of a particular commodity while allocatng foreign exchange and have favoured some at the cost of others Germany for instance gained substantial commercial advantages by shrewd bargaining with the help of exchange

control She used exchange control *to facilitate economic* penetration in the neighbouring countries, particularly those of the South-Eastern Europe

7 *To Plan the Economic System.*—Exchange rationing is used to plan the economic structure of the country so as to reduce its dependence on the foreign supplies The desire for autarchy and military power have led to the introduction of '*steered economy*' *In its working* exchange control has recorded a marked success in this direction The entire economic structure of Germany has been regimented[1] and reshaped and its military machine renovated with the assistance of exchange control *Both the strength and vulnerability* of the new German economic system is largely due to exchange control.

Important Methods of Applying Exchange Control

1 **Use of more than one Rate of Exchange.**—In certain countries the official rate of exchange is available only for certain purposes, and the rest of the transactions are allowed at a discount over the official rate Several of the South American countries have more than one rate of exchange for their currencies Argentine has an official rate for dealings in foreign exchange derived from regular exports, and a "free" rate for foreign exchange derived from supplementary exports Same is the case with Bulgaria Bolivia Brazil Chile, Columbia and Uruguay This method is more elastic than the policy of vigorous centralisation under government authorities Germany has followed the practice of rigid centralised control This partial recognition of the unofficial market is due to the desire to permit capital movements and impart flexibility in exchange regulations For instance in Bulgaria the exporters after surrendering a certain percentage of their foreign exchange at the official rate were authorised to sell the remainder in the free market, which they did at a substantial premium In

1 "At the present time the private entrepreneur would not be allowed to undertake new investment if he desired to do so Only strategic industries may have exchange for imports of raw materials only firms filling orders for military supplies and autarchic substitutes for foreign finished goods may tap the supplies of skilled labour and capital" Vide Poole K. E. German Financial Policies 1932-39" p 6

Argentine there were two recognised rates for the peso. The official rate, which applied to dealings in foreign exchange derived from regular exports, was stabilised at 15 pesos to the pound sterling in January 1934 for the purchase of foreign currency and at 17 02 pesos to the pound sterling for sales The "free" rate was applicable to foreign exchange derived from supplementary exports, liquidation of "blocked" accounts, etc In December 1936 the official selling rate was reduced to 16 pesos to pound sterling After the introduction of exchange control in October 1931, Bolivia had two and sometimes three rates of exchange for its national currency A Decree issued in January 1935 established two legal rates the official rate and the export rate Further, it determined the percentage of foreign exchange, varying according to commodities, which exporters were required to sell to the Banco Central de Bolivia at the official rate and the export rate In Brazil, according to the Decree of February 1935, 65 per cent of of the foreign exchange derived from exports was permitted to be sold at the free rate and the remainder was to be handed over to the Banco de Brazil at the official rate In Chile there were four rates of exchange the official rate, export rates, compensation rates and free rates Colombia had two rates for the peso the official rate and the free rate

2 **Subsidies on Exports and Restrictions on Imports**—In certain cases, the exchange control regulations permit special concessions to particular commodities for export markets and to special countries These concessions are intended to promote export trade and in respect of definite commodities So long as there were a number of countries with free currencies, exports to these countries were bound to bring to the exporter a "healthier" currency, for which the authorities were prepared to pay a higher price, not merely to encourage exports to these countries, but also to have more free exchange Hence premia over the official rate were allowed in these cases The premia over the

official rate allowed to exporters varied according to commodities and the countries of destination. The importers were required to pay surcharges over the official rate, in order to deter them from purchasing abroad. Selective rationing of foreign exchange was resorted to. Here the object is to secure an improved balance of trade and more foreign exchange by restricting non-essential imports and encouraging exports. For instance, according to the exchange control regulation introduced in Hungary, the National Bank of Hungary allowed premia on the foreign exchange handed over to it by exporters, and levied surcharge on the foreign exchange allotted to importers. The amounts of such premium and surcharge rates originally varied in accordance with the class of commodity dealt in, and with the country of origin from which the goods were imported or the country of destination to which they were being exported. In December 1935, however, the rates were unified at 50 per cent. for premia and 53 per cent. for surcharges, with the exception of certain countries for which lower rates were fixed. In Rumania, the National Bank gave premia to exporters varying from 10 to 40 per cent. from June 1935 and imposed a surcharge of 44 per cent. on importers. In December 1935 the various premia were replaced by one single premium rate amounting to 38 per cent. of the official exchange rate, in the case of currencies that were not subject to any restriction, and an ad valorem tax of 12 per cent. was imposed on all imports.

Blocked Accounts used to Aid German Exports.—Germany has developed and perfected the system of blocked accounts in order to aid, inter alia, German export trade. To be able to understand the implications of this system, which is an important part of the German exchange control mechanism, it is essential to trace the origin and analyse the methods of utilisation. We will, therefore, explain the nature of different kinds of blocked marks.

I **Free Reichsmark Account**[1] —These are accounts created since July 1931 at a German bank by a foreigner in his name from the proceeds of the sale of foreign currency, which he himself has paid in, or which has been paid in by another foreigner, or by a resident in Germany with the permission of Foreign Exchange Authorities The foreign owner can freely dispose of such an account within Germany The exchange of a free Reichsbank credit into foreign currency cannot be effected without the permission of Foreign Exchange Authorities

II **Credit Blocked Accounts** —These are created by (a) proceeds from the sale of inland property (b) proceeds from the repayment of loans mortgages etc which were granted by a foreigner before the 16th July 1931 (in the case of a foreign bank before the 9th October 1931) and which are not governed by a Standstill Agreement Credit blocked accounts can without permission be used to purchase German Reichsmark securities with certain exceptions Every other withdrawal needs the written approval of the Foreign Exchange Office which will as a rule be given for the following purposes —(i) For long term investment in Germany such as on mortgages purchase of real property etc If the mortgage is repaid or the property is sold the proceeds must be paid back into a credit blocked account again (ii) To pay expenses of a non business journey in Germany of the original holder of the account members of his family and suite up to a maximum of R M 2 000 per person per month The journey may only be for holiday or health reasons and the amount released must actually be used for travelling expenses within Germany These accounts may also be used for the expense of a stay for study purposes but not for business purposes (iii) Gifts by the original holder of the account for personal assistance of relations or for subscription to social religious or other bodies or for appropriate grants to persons entitled to assistance in Germany (iv) Payment to German residents of costs connected with the creation or administration

1 V de Rawlins E. C. D Economic Conditions in Germany pp 31 36

of the blocked account (court fees, legal charges, bank charges, etc) (v) Payment of taxes of the original holder of the account (vi) For payment of 25 per cent of the invoice price of new orders of German goods or for services of firms in Germany for the account of the original holder of the account The remaining 75 per cent of the invoice must be paid in foreign currency or free Reichsmarks Permission to use blocked credits in this way is not given for goods to be exported to the U K Finland, France Italy, the Netherlands Austria, Rumania or Switzerland, owing to the Payment or Clearing Agreements entered into with these countries

III. Note Blocked Account.—These are created by the Reichsmark Notes which are sent to Germany with instructions to pay them into a blocked account Under a law dated 6th December 1935 it is forbidden to bring Reichsmark Notes into Germany from abroad to an amount exceeding R.M 30, except for payment into such a blocked account These accounts can, without permission, be used to purchase German securities with certain exceptions With the permission of the Foreign Exchange Authorities these accounts may be used to a limited extent (a) for loans on mortgages or loans to residents in Germany for participation in German firms or companies in each case for at least five years, (b) for part of the purchase price of real property Dealings in the property can only be effected by permission of the Foreign Exchange Authorities Further these accounts are in principle on the same footing as credit blocked accounts held by a person other than the original holder If real property is purchased with these notes 50 per cent of the price must be paid in foreign currency, and in the case of new buildings at least 25 per cent of the costs must be provided in foreign currency

IV Old Credits.—These are bank deposits of a foreigner in Reichsmark or foreign currency which existed prior to the 16th July, 1931 and which are not the subject of a Standstill Agreement These accounts can be utilised in the

same manner as credit blocked accounts, except that only 25 per cent of the amount standing in the account on the 1st April, 1932, can be dealt with unless the Bank at which the Account is held gives permission for the utilisation of a further 25 per cent

V. Emigrant Credit Account.—These are credits in a bank of a person who has given up his residence in Germany and removed abroad since the 3rd August, 1931 Repayments of loans, payments of claims, proceeds of sale of property which accrue after emigration are also paid into the Emigrant Credit Account These accounts can be operated in the same manner as credit blocked accounts

VI. Securities Blocked Accounts.—These arise from proceeds of sale of securities (except German Foreign Loans). Where the blocked accounts arise from proceeds of securities which were the property of the foreign owner on the 15th April, 1932, it may be utilised roughly in the same manner as credit blocked accounts Security blocked accounts which have been brought or otherwise acquired since the above mentioned date, cannot be used to purchase long-term investments other than German inland shares and securities

VII. Special Blocked Accounts—With the permission of the Foreign Exchange Authorities, interest and dividends, rents and other similar regular payments, as well as regular amortisation payments from deposits, credits, mortgages, participations in firms, or loans, may to an appropriate amount be paid into a special account in a bank authorised to deal in foreign exchange Special blocked accounts may be used by the foreign owner of the account for making the following payments (a) gifts to relatives for personal financial assistance, or to social, religious or other societies, or for an appropriate amount to persons in Germany with a proper claim to support, (b) for services rendered by German residents in connection with the creation and administration of the account or other blocked money or property in Germany, (c) payment of taxes on the holder's

capital or income in Germany, (d) travelling expenses on a non-business holiday in Germany for the holder, members of his family and accompanying servants up to R M 2 000 per person per month The Foreign Exchange Authorities may authorise other payments within Germany but not payments for goods, nor for loans or investment in landed property or in business

VIII Conversion Office Credits—These are created by payments of interest, dividends, regular payments arising from deposits, credits, loans, mortgages, participations in business and other investments of foreigners in Germany where the capital was in Germany before 16th July, 1931 Payments have normally to be made by the German debtor to the Conversion Office In respect, of interest, etc, (but not amortisation) payments received, the Conversion Office offers British creditors 4 per cent Funding Bonds maturing on the 1st January, 1945, on the understanding that the acceptance of the Funding Bonds is in full settlement of any coupons etc, funded Where a foreign creditor does not wish to accept Funding Bonds his credit in Reichsmarks remains with the Conversion Office, but earns no interest In special cases permission can be given to use these credits for payments within Germany for taxes, non-business travelling expenses or gifts to needy relatives

IX. Clearing Agreement Accounts—Germany has concluded clearing agreements with the more important countries These agreements provide for a mutual clearing of the claims for exports Payments in Reichsmarks is made into the Reichsbank to the credit of the National Bank of countries with which clearing agreements have been made for imports from those countries The Reichsmark credits are then used to pay German exporters for their exports to the same countries A similar procedure is followed in the other country Conversions between Reichsmarks and the currency of the other country are made at the official rate of exchange in the case of strict clearings but there are some exceptions where the Reichsmarks are disposed of at a discount

X. Foreigner's Special Accounts for Inland Payments (ASKI).—These accounts are opened at German banks with the permission of the Foreign Exchange Authorities in the names of foreign firms trading with Germany for the acceptance of Reichsmarks in payment of exports to Germany The foreign firms are then allowed to pay for one-third of the value of German goods which they purchase from credits in the account on condition that the balance is paid in free foreign currency This form of account is no longer permitted in Anglo-German trade, and is restricted to very small classes of goods in trade to many other countries With certain foreign countries, however, Aski accounts are used as the basis of the entire mutual trade, and the Aski-Marks are normally sold at a discount

XI. Register Mark Credits—These arise out of short term credits made by foreign banks before the 1931 crisis, which are subject to Standstill Agreements between the foreign bank creditors and the German banks and other debtors These credits can, under certain conditions, be called up for payment in Marks, called Register Marks Register Mark Credits can be utilised for investment within Germany, for tourist expenses and for certain other purposes

XII Tourist Special Accounts—According to regulations issued by the Reichsbank, foreign bank credits and other authorised institutions, including foreign travel agencies, may acquire Register Marks, pay them into Tourist Special Accounts, and sell "Travel Cheques" or letters of credit drawn on these accounts to foreign travellers to Germany The latter may cash such cheques in Germany up to an amount of R M 50 per day, in special cases where a letter of recommendation is granted R M 100 per day may be drawn Marks obtained by cashing these cheques may only be used within Germany and for the following purposes:
(a) Fares on German railways, motor traffic concerns and inland shipping companies for journeys within Germany
(b) Reservation of accommodation on German and foreign marine and air vessels for journeys to and from Germany

(c) For hotel and other expenses Foreigners staying in Germany for study purposes may, with special permission, draw Register or Travel Marks Register or Travel Marks not spent before leaving the country must be sold to a foreign exchange bank. They cannot be taken out of the country

XIII. "Non-interest Bearing Reichsmark Trustee Credits and "Tourist Special Account II".—Interest payments on Dawes and Young Loans in so far as they are not dealt with in Transfer Agreements made with different countries may be paid into a non-interest bearing account in Berlin Credits in this account may be used with the permission of the Reichsbank, for the following purposes —(1) For the purchase of German bonds and shares which are quoted on a German Stock Exchange in terms of Reichsmarks (2) For investment in long-term loans and mortgages (3) For the acquisition of landed property within Germany or for other property with the approval of the Reichsbank. (4) For payments of expenses for a temporary visit in Germany

From the foregoing review it will be seen that German Government has built up a complicated method of blocked accounts to aid German economic recovery and export trade and to increase the stock of foreign exchange at its disposal. The prohibition under foreign exchange regulations of the repayment of capital sums due to foreigners and a complete moratorium on interest payments depressed the prices of all German securities and property rights held by foreigners abroad But these very securities remained at full, or, at any rate, greater value to residents in Germany who could receive payment of the whole interest and therefore the price quoted in Germany were much higher than abroad German firms wishing to sell goods on the world market, but finding it impossible to do so owing to lower prices of competing foreign firms could, with the permission of foreign exchange authorities purchase German bonds or shares with foreign exchange at the depreciated foreign market figure, repatriate them, and sell them at a profit on the home market, the profit being used to compensate the

German firm for loss on export transaction Similarly, these blocked accounts could be bought up by the German firms at a heavy discount, and the profits made on such transactions, which could only be carried out with the permission of foreign exchange authorities, had to be devoted to subsidise exports Great Britain is also building up "special' or "Registered" accounts and the "free" sterling market is rapidly disappearing

"Scrip Certificates" were used to encourage German exports Under the German Moratorium Law of June 1933 regular payments on long and medium term loans, mortgages, investments, etc, due from German Nationals to foreigners had to be made in Reichsmarks into a "Conversion Office"[1] Out of this Reichsmark fund up to the end of 1933 half the amount owed was transferred to the foreign creditor in his own currency, for the other half he was given 'Scrip Certificates" The proportion alloted in foreign currency was gradually reduced The scrip certificates were repurchased abroad by bank agents of the German Gold Discount Bank at half their face value The profit made on these transactions was used to subsidise exports which, but for a subsidy, could not compete with foreign goods on the world market[2] Notwithstanding the inducement, German exports declined from 13 480 R M in 1929 to 5,260 R M in 1938

Restrictions on Imports into Germany—Under the system of foreign exchange control in force from 1931 to September 1934, German importers were given a free foreign exchange allotment in proportion to the imports before 1931 Within this allotment they could pay for imports in their own line of business This system broke down completely in June 1934, when the quota granted to importers had been progressively reduced between February and May from 50 per cent to 5 per cent of the original figure and finally to day-to-day allotment based on the Reichsbank's intake of foreign

1 Dealings in blocked marks were tightened up and centralised in this office and in the Gold Discount Bank Since October 1933 owners of blocked and registered marks had to offer them through the Conversion Office to the Gold Discount Bank which bought them at the current discount and used them in assist ng exports

2 Vide Rawlins L C D Economic Conditions in Germany 1936 p 157

lats to the pound sterling, was legally linked to sterling at a rate of 25 22 lats to the pound This led to depreciation of the lat [1] The German authorities took special measures to counter the depreciation of Mark [2] But the system of "blocked" marks enabled them to initiate a peculiar type of depreciation of their currency Dr Schacht resorted to disguised and differential method of depreciation by creating different types of Marks for stimulating German exports at the cost of foreign investor Under *the circumstances, there were two ways open to* Germany to maintain her foreign trade and safeguard her balance of payments, one of internal deflation by cutting costs and prices and the other to depreciate the exchange rate of the Mark Dr Bruning had selected the method of deflation But Dr Schacht, as the Minister of Economics under the National Socialist Government, selected the latter alternative to mitigate unemployment He resorted to inflationary finance of an extensive scheme of public works huge rearmament programme, labour camps etc This led to higher wages and increased thereby the wages bill of the industry Thus the cost and price structure recorded a marked upward trend Under such conditions German exports could not compete in the world market and had to be subsidised with the help of "blocked marks" This practice was also followed by a number of countries in Europe and in Latin America although Germany is most important Since England went off the gold standard in September 1931, the currency system of several countries were faced with increasing difficulties The countries thus affected tried to maintain the stability of their currencies by controlling the transfer of funds abroad At the same time strenuous efforts were made to acquire more foreign exchange The ingenious method of "blocked" Marks enabled Germany to reap in full the advantages of currency depreciation and at the same time to

sustain the fiction that she was still adhering to the gold standard by maintaining the nominal parity of the Mark[1]

4 Restrictions on the Export of Capital—Due largely to depression and the economic policy pursued by the creditor countries the currency systems of the debtor countries were subjected to heavy strain Capital tended to flow out due to political and psychological reasons Discount policy could not be effective in reversing the flow To prevent the financial system from utter collapse these debtor countries in particular were anxious to check the outward flow of funds For instance German Government in the earlier stages tried to check the flow and subsequently in 1934 prohibited export of capital and effectively regulated foreign exchange transactions by an extensive and centralised administration All claims of foreigners were 'blocked' and an intricate system of "blocked accounts" was built up The transfer restrictions were found inadequate in effectively stopping the efflux of funds and had therefore, to be supplemented by the blocked currency system which definitely regulated the transfer of funds In November, 1940, Britain also announced the existence of "blocked sterling"

This system is usually adopted by the debtor countries Under the system, the Government of the debtor country permits its citizens to pay their foreign debts in national currency into a special blocked account In some cases such settlement is not compulsory, and the foreign creditor has to make his choice between the payment through the blocked account and the risk of the depreciation of the debtor's national currency

It is essential to note at this stage that the payment by the debtor into a "blocked" account does not alter the international indebtedness between the two countries So also the resources of the account are frequently drawn upon directly and indirectly for internal use, both for state

1 "The disparity between German prices and other gold prices has now become so wide that the internal economic situation of Germany has become exceedingly difficult In spite of the partial depreciation of the mark, Germany is finding it more and more difficult to effect sufficient exports to buy the raw materials required to keep her population in employment even on a diminished standard of living" Vide Harris, C R S, p 83-84

and private purposes When thus utilised, the blocked balances may conceal the insolvency of the debtors and more so if used for the purposes of the State Thus, the system provides very slender security to the creditors Therefore, we find that most of the holders of blocked balances are prepared to sell their claims at a substantial loss; the prices of various types of blocked currencies differ If the policy guiding the system is conservative, it produces moderately deflationary effect on credit Where the blocked balances are employed, directly or indirectly, they have an inflationary effect

Further, to prevent the export of capital, export of domestic currencies, bank notes and precious metals, except in strictly limited amounts, is forbidden Close watch is invariably exercised on all citizens and residents going abroad in order to find out the nature of assets they are taking with them abroad On their return they are required to make a statement on oath of their expenditure abroad The rights of the non-nationals to dispose of their assets in exchange control countries is also restricted Foreigners passing through the country have to declare the foreign currency they possess and they are not allowed when leaving the country to take with them amount higher than the sum declared These restrictions check surreptitious transfers of capital to foreign countries

5. Control and Supervision of all Commercial Transactions.—To prevent withdrawals of capital, the debtor countries had to institute a comprehensive control of commercial transactions The development of Control Boards in Germany, under Dr Schacht since 1934, shows the character and complexity of such organisation intended to secure an effective control This complicated and costly organisation had to be built up because the export of capital may be disguised through commodity exports Exporters, for example, may enter lower prices for their exports in their invoices and thereby keep a portion of their proceeds abroad Similarly,

importers may arrange with the exporters to quote higher prices for the goods and the difference may be kept at the foreign centres To prevent such evasion and a consequent flight in goods it was necessary to build up an extensive organisation so as to enable the control authorities to check every transaction very carefully *After* the *declaration* of War in September 1939, Great Britain has also adopted rationing type of exchange control with rigid methods The Order of November 23, 1939, made special provision for the strict control of the invoicing exports and increased the penalties for false declarations, to counter the subtler moves of the evader and stop a loophole through the exchange control which Continental experience had proved to be dangerous Britain has profited from the German experience of strict exchange control The latest British regulations expressly forbid various forms of evasion and export of capital by way of "compensation", of which the simplest and most familiar example is the payment by a resident in his country of a non-resident's debt against the payment of foreign currency to a third party by the non-resident in his own country

6 **Compulsory Surrender by Nationals of their Foreign Exchange Holdings.**—When a country introduces exchange control it requires its nationals to report to the authorities, usually the Central Bank, their holdings of foreign securities bank balances abroad, claims and liquid assets in general, and even real estate Sale or transfer of these assets is regulated When necessary, the Government may call upon the nationals to surrender these holdings to the central bank of the country The nationals are paid their claims in domestic currency To be effective, these rules must be enforced scrupulously and honestly, the supervision should be very close Germany has used this method successfully Great Britain has also adopted it after the declaration of War

7 **Bilateral Balancing of Trade.**—It has already been shown that by 1934 German Government was faced with an extreme shortage of foreign exchange and had to declare

a complete moratorium on Germany's long-term and medium-term debts, including Dawes and Young loans The most important cause which led to this grave crisis in Germany's financial structure was the adverse balance of trade. An export surplus of R M 665m in 1933 was converted into an import surplus of R M 284m in 1934 The gold and foreign exchange reserves of the Reichsbank dwindled in the course of the year from R M 396m to R M 84m The German Government, therefore, had to rearrange her trade relations on the bilateral basis Direct and specific barter transactions were entered into by the German Government with other countries For instance, in October 1938 Turkey was granted a credit of 150 million Marks, to be repaid in Turkish primary products In the same month Poland was given large credit on similar terms In January 1939, Bolivia agreed to accept German machinery, valued at about 4 million Marks, against Bolivian petrol and minerals Similarly, with Argentine, she negotiated an agreement bartering 14 million Pesos worth of German railway equipment for Argentine wheat worth 8 million Pesos and wool worth 8 millon Pesos

Clearing Agreements—The institution of clearing agreements[1] was developed in its modern form during the days of the depression These were the days of excessive tariff barriers, quotas, imperial preference, exchange restrictions etc The most obvious result of all these measures was a distortion of the normal channels of international trade and its restriction In their initial stages all these measures had assumed the garb of self-defence, only to be seen in their true colours too soon Their protogonists knew well enough that once established these measures create vested interests No wonder, therefore, that these measures have tended to perpetuate themselves and created new economic problems

of their own The international trade is therefore moving in artificial channels financial difficulties have multiplied, currency instability has undermined international confidence, and defaults in payments are very common

It has already been pointed out that in view of the rapidly increasing shortage of foreign exchange, certain countries had felt it necessary to limit, or entirely suspend, transfer abroad in respect of financial obligations and to limit the power of private individuals to purchase the foreign exchange required to pay for imports The monetary authorities discriminated between several imports and the claims of most essential ones were given preference The result was an accumulation of 'frozen' commercial claims Besides, the regulations and restrictions of imports adversely affected the trade of exporting countries Further, the creditor countries and the other exporters whose commercial claims had remained unpaid were reluctant to accept payment in the form of increased imports from the debtor countries Under these circumstances the countries whose claims remained unpaid thought of devising a system which would enable them (1) to obtain payment for goods already delivered (2) to continue as far as possible—even on a reduced scale—their exports to the country in question, and (3) to secure at least partial repayment of their financial claims[1] The debtor countries on the contrary, wanted a system which would protect their economic system from collapse and at the same time enable them to discharge their obligations The system of clearing agreements was devised as a compromise to find an escape from the impasse

It is argued some times that the clearing system is similar to clearing house system of set-off operations adopted by banks It is necessary therefore to emphasise the difference between the normal banking system of clearing and the clearing that takes place under these agreements The normal system of clearing can only operate between countries in which foreign exchange transactions and currency

1 Vide Report of Enquiry into Clearing Agreements (League of Nations) p 11
Einzig P "The Exchange Clearing System" pp. 61-62

movements are not restricted Debits and credits between each country and abroad are set off spontaneously and automatically by the method of exchange of credit instruments, calculated at free world-market rates, in certain institutions that are specially engaged in such transactions Clearing is a banking matter, pure and simple Importers and exporters are not concerned at all in the matter, they are entirely free and there is no compulsion upon them But the set-off financial operations associated with the clearing agreements are materially different There is compulsion upon both importers and exporters and international payments are rigidly regulated Further the clearing agreements are usually strictly bilateral whereas under the normal system the arrangements are trilateral or multilateral Again clearing agreements are often based on artificial rates of exchange entail rigid regulations and turn the countries into self contained units Besides individual states that are parties to clearing agreements unable to secure an automatic equilibrium in their balance of payments, are trying to secure a separate equilibrium with each country by concluding such agreements This arrangement distorts the channels of international trade and restricts its flow

German Clearing Agreements—The primary object of the German clearing agreements was to ensure that while maintaining the level of trade the exporters in the countries concerned should have a first claim on the proceeds of German exports to their country and that the proceeds of Germany's export surplus should be devoted to paying arrears of trade debts and interest to their nationals who held the German bonds[1] The original purpose of earlier German clearing agreements was to enable foreign trade to carry on in spite of lack of foreign exchange Germany entered into clearing agreements with countries which were suffering with the shortage of foreign exchange with the intention of thawing Germany's frozen credits there provided Germany's balance of trade with them was normally

unfavourable Thus out of the effort to render foreign trade possible, in spite of the lack of foreign exchange there grew up the tendency to cut out altogether if possible, the transfer of foreign exchange in foreign trade It is this trend that has given the clearing agreements their modern form. In those cases where Germany attempted at thawing the frozen credits clearing agreements were coupled with payments agreements

Procedure of Clearing Agreements.—The normal procedure of the clearing agreements may be noted The underlying principle of the system is that each contracting country collects the trade debts owed by its nationals to the nationals of the other in its own currency the importers paying their debts to the Central Bank The claims are offset without the assistance of foreign exchange except in the case of excess of imports over exports For instance let us suppose that there is a clearing agreement between Germany and Netherlands Then all Dutch importers of German goods would be required to pay the sums due to their German suppliers in guilders into a special account at the Netherlands Bank and all German importers of Dutch goods would have to pay the sums due to their Dutch suppliers in Reichsmarks into a special account at the Reichsbank Thereafter each central bank pays the claims owing to its nationals in its own currency and the balance if any is credited to the party to whom it belongs Now since Germany normally exports more to Holland than Holland does to Germany the guilders in the Account would be more than sufficient to cover the claims of Dutch exporters to Germany, the balance can be used according to the terms of the Agreement to pay off 'frozen debts owed to Dutch nationals and the Duch holders of German bonds and the balance left over could be handed over to the Reichsbank.

Technique of Clearing Agreements —

1 **Order of Payments to the Exporters.**—As a gentle rule the exporters are paid out of the funds available in the clearing account in the chronological order of payments

made by the debtors But in some clearing agreements priority is given to certain class of exporters to encourage a particular class of exports Priority, thus accorded, may be either over all receipts of the clearing accounts or over receipts from a certain source For instance, according to the Swiss-German Clearing Agreement, foreign exchange to German tourists in Switzerland was provided out of the proceeds of the German exports of coal to Switzerland which were reserved for that purpose This arrangement was continued after the Agreement was renewed in April 1935 These reservations are rare and payments are generally made in chronological order

2. Advances to Exporters—In certain cases exporters are given advances pending the clearance of their claims to encourage exports of that particular class For instance, first German-Hungarian Clearing Agreement provided for advances to the German exporters up to 50 per cent of their claims

3. Allocation of Funds—Clearing agreements also provide for the distribution of funds amongst classes of claims current exports, financial arrears, and investors' claims In some cases definite percentages are laid down For instance the Swiss-German Clearing Agreement provided that out of the balance in her favour Germany would pay in full the interest on the Dawes and Young Loans and interest on other bonds up to 4½ per cent In those cases where the interest due exceeds 4½ per cent half of this excess amount was also to be similarly paid for the remaining half being "blocked" in Germany The holders of private claims were to receive interest up to 4½ per cent the difference to be utilised for redemption purposes Their agreement however, did not work satisfactorily and increased the arrears of claims Therefore a new agreement was entered into in April 1935 This agreement provided for detailed distribution of assets It laid down that out of the first 19 6 m Swiss francs of German monthly exports to Switzerland, excluding coal, provision would be made for trade payments in respect of current Swiss exports and other charges

and one million Swiss francs would be reserved for the repayment to Swiss banks of the advances they had made to Swiss holders of investments in Germany under the old transfer agreement, and of any surplus above 19 6m. Swiss francs, 60 per cent was to be used for further repayment of advances and for current payments to Swiss holders of investments in Germany The cash available was to be used to pay interest up to 4½ per cent on Swiss holdings of Dawes and Young Loans and holdings held in Swiss francs to be given preference in this respect Any amount of interest not paid in cash were to be paid in 4 per cent Swiss franc funding bonds Thus current exports were given first preference and a definite sum fixed for payment Then came the investments and Dawes and Young Loans

The German Dutch Clearing Agreement of June 1935 is equally interesting in this respect It provided for cash payments to be made to Dutch holders out of the proceeds of certain additional German exports to Holland Interest on bonds or dividends were to be paid under this agreement up to 3½ per cent and rents upto four-fifth of their amount In respect of amounts due in excess of these limits and upto a total of 5½ per cent interest, Dutch holders were given the option of 4 per cent Gulden funding bonds or "blocked marks" which the recipients could use for their own travelling and personal expenditure in Germany or to meet certain other liabilities in Germany These Mark credits could not be transferred to other people and became known as 'Holland Marks' As regards the Dawes and Young Loans interest in excess of 3½ per cent was to be paid in "blocked marks' ('Dawes and "Young Marks) which were practically equal to register marks The Agreement further provided that Dutch tourists purchasing 'register marks" or "Dawes' or "Young" marks must at the same time purchase a certain proportion of free marks the proceeds of which to be credited to the Dutch clearing account

According to the Swedish German Clearing Agreement of July 1935 50 per cent of the proceeds of German exports to Sweden were to be set aside to pay full interest on the

Swedish holdings of the Dawes and Young Loans and the interest on the Swedish holdings of the Kreugar Loan The surplus, if any, was to be used for repayment of interest up to 4½ per cent in respect of non-Reichs debt, dividends up to 4½ per cent plus half the excess due, and rents in full Failing this holders of non-Reichs debts could receive "blocked marks" up to 6 per cent interest, which might be used for the holders' own journeys in Germany on business or pleasure, and for meeting certain other liabilities in Germany These "Swedish Marks" were similar to the "Holland Marks" noted in the preceding paragraph

4. **Provision for Conversion of Currencies**—The clearing agreements generally make provision for conversion of the currencies because invoice is usually made out in the currency of the seller When an invoice is thus made out it must be converted in the currency of the buyer, since the latter, if exchange control is in force, pays into the clearing fund of his country in his national currency To be able to pay in his own currency, the importer must know the rate at which the currency of the exporter could be converted into his national currency Same is the case when the invoice is made in a third country's currency The following bases[1] for conversion have been used (1) legal gold parity, (2) official rate of exchange, (3) conventional rates, (4) market rates, (5) mean rate of the day in a given course, (6) a stable currency of a third country

In most of the clearing agreements entered into in the earlier stages the legal gold parity was used as a basis for conversion But it created serious complications in the countries with depreciated currencies Some of the agreements therefore broke down The basis of conversion had therefore to be changed

The official rate of exchange, where it is used as a basis of conversion of currencies, is determined by the exchange

1 Vide Enquiry into Clearing Agreements (193.) pp 32 33

control authorities This arrangement may work satisfactorily so long as the official rate of exchange represents the equilibrium rate of exchange But it must create complications where the exchange control authorities try to adjust the official rate of exchange in such a way as to allow the national currency to depreciate in terms of the currency of the other contracting party This sort of exchange depreciation would penalise imports

Where the system of exchange control has been developed extensively and is used to regulate foreign payments in such wise as to encourage export trade, the national currency suffers a substantial depreciation in terms of the foreign currency To secure their objective effectively, the exchange control authorities in these countries fix a rate of conversion suited to their requirements For instance, in Germany, where exchange control is centralised, the authorities fix the conversion rate at a convenient level in harmony with their general commercial policy Such rates of conversion must distort the channels of trade and check the flow To prevent this unhealthy development, the creditor countries usually demand adequate safeguards and put definite checks on the powers of control authorities Sometimes, the clearing institutions themselves are authorised to fix the rate of exchange from time to time Under this arrangement, if properly worked the exchange rates would be more akin to equilibrium rates and promote the flow of international trade in right channels

Sometimes the clearing agreements provide that conversion of currencies shall take place at the market rate, or mean rate of the days on a given course In such cases authorities are left with very little discretion to directly manipulate the exchange rates The rate thus determined is almost a free market rate If exchange rates are permitted free play they would reflect more truly the internal cost and price structure in the countries concerned Another important basis used for conversion is a stable currency of a third country This method is less arbitrary and the rate

thus determined will be closer to the equilibrium rate than the officially determined rate in countries where exchange control is in force

5 **Surplus Balance in Clearing Accounts**—The clearing agreements also make specific provision for the use of surplus in the clearing accounts which may remain after a certain period or at the time of the termination of the agreement In some agreements the right of disposal of the surplus is given to the party in whose favour it may arise in others the debtor country in whose favour the surplus has arisen has to use it to expedite the settlements of debts In certain cases the discretion as regards the distribution of the surplus in vested in both clearing institutions it can be disposed by mutual consent As regards the balance remaining at the expiration of the agreement a liquidation clause provides that importers with the favourable balance must continue to pay to the clearing house until the claims corresponding to such balance have been met in full But even when such a liquidation clause is not explicitly incorporated in the clearing agreement the method adopted for liquidating the balance is to increase the exports of the country which is a debtor on the clearing account

Triangular Clearings—Most of the clearing agreements are bilateral But there are a few cases of triangular arrangements Triangular clearing agreement is an arrangement between three countries by which the debit balance in the clearing account of a country (say 'A') against another country (say 'B') can be offset against its (i e A s) credit balance or its clearing account with a third country (say 'C) The scope for such tripartite or multilateral clearing agreements is strictly limited at the present and will remain so in future so long as advanced countries continue to follow short-sighted aggressive economic policy

Classification of Clearing Agreements —

1 **Pure Clearing Agreements**—We have already analysed in detail in the preceding section this category of clearing agreements The importers have to say their debts in

national currency and exporters collect their debts also in national currency Transfer of foreign exchange is thus eliminated. Further in each of the contracting countries a special organisation is asked to receive in national currency the sums paid in by importers and to pay exporters from this fund, provided that in the other country the importers have paid the amounts they owe The sums paid into the different accounts do not bear interest But it is essential to note at this stage that in some cases the clearing system is established on a voluntary basis while in others it is compulsory In case the basis is voluntary the traders of the contracting countries are not compelled by law to make payment through the clearing office To this class belongs the Anglo German Agreement which came into force in August 1934 This agreement was intended merely to cover current trade and the question of accumulated arrears of payments was expressly excluded from it and left to be dealt with by separate negotiation Thus German importers of British goods who found that the sums in foreign exchange alloted to them by the German Exchange Control were in sufficient to pay for the goods they had purchased were permitted to pay the balance in Reichsmarks into a special (Sondermark) fund at the Reichsbank to be opened in the name of the Bank of England The Reichsbank was given powers in order to protect its exchange reserve from too sudden drains to suspend the acceptance of Reichsmarks into this fund whenever the Sondermarks accumulated in the account exceeded RM 5 millions until they had fallen below that total The Bank of England was permitted to dispose of the Sondermarks at any time for the purpose of making payments in Germany for goods exported from Germany to the U K or for effecting other payments in Germany approved by the Reichsbank This Agreement was only a partial success It was discovered in practice that the Bank of England had considerable difficulties in disposing of the Sondermarks on the London money market and the fund quickly filled beyond its maximum of RM 5 millions so that the Reichsbank was constantly suspending the acceptance of Reichsmarks into the

Sondermark fund, with the result that considerable delays in payments in sterling occurred The British importers of German goods made comparatively little use of Sondermarks to meet their commitments in Germany The chief obstacle to their employment seems to have been the custom of German exporters of invoicing their goods in sterling rather than in marks It was discovered that notwithstanding the strongest control over the internal costs and income of the country certain German exporters were prepared to quote lower prices for sterling than for Sondermarks The greatest weakness of the Sondermark Agreement was its voluntary basis British importers of German goods were permitted to continue to make payments either in sterling or in 'free' marks and the only inducement to them to adopt the new method of payment was the fact that Sondermarks were slightly cheaper than 'free' marks But the discount offered by the Bank of England of about 2 per cent was not a sufficient inducement to popularise the Sondermarks with British importers of German goods Moreover a considerable volume of Germany's import trade was excluded from the Agreement which was not to apply to imports over which the German Government exercised special control Further the Agreement did not deal with the growing problem of the German trade debts which had already accumulated Frequent complaints were made in British business circles of the failure of German importers of British goods to make payments for them when they fell due owing to their inability to obtain the requisite foreign exchange Therefore a new agreement was concluded in November 1934 The experience of exchange clearing on voluntary basis was discouraging On the other hand compulsory exchange clearing has proved more successful and is therefore quite popular

2. **Clearing and Payments Agreements** —This type of agreements differ from the pure clearing agreements in that in addition to the important clauses contained in the latter category as noted above they have one or both of the following provisions (a) In the country which has not

introduced foreign exchange control, a certain percentage of the sums paid by the importers is placed at the free disposal of the central bank of the other contracting country, for the payment of the trade debts contracted prior to the conclusion of the agreement, and for the authorisation of debts other than trade debts (public debts or private debts of a financial nature), or for any other purpose The balance alone is reserved for the payment of exports subsequent to the conclusion of the agreement (b) In the country which has introduced foreign exchange control, outstanding trade debts to the other contracting country are paid to exporters by importers themselves by means of direct transfer of foreign exchange placed at their disposal by the central bank

3 Payments Agreements —These are agreements[1] entered into between two countries one of which has introduced exchange control and the other has not Under this category of agreements, a country which has introduced exchange control undertakes to authorise its importers to make a direct transfer of foreign exchange to the account of the exporters of another contracting country without exchange control up to a certain amount fixed in the agreement of the total amount of foreign exchange transferred by the latter country for the payment of its current trade debts to the former country A country with exchange control also undertakes to reserve a certain percentage of the total amount of foreign exchange transferred by the country without exchange control for the amortisation of one of the following categories of debts which it has contracted with the latter (a) trade debts, prior to the conclusion of the agreement, or (b) debts other than trade debts (public debts or private debts of a financial nature), or (c) debts mentioned under (a) and (b) To this class belong the Anglo-German Payments Agreement concluded in November 1934 The main principle underlying this arrangement was the linking together of import permits and foreign exchange

1 "It was designed not simply to liquidate blocked balances as was the exchange—clearing arrangement, but also to meet the problem of current debt service on international financial obligations and it has also been employed to give preferential trade treatment" Vide Gantenbein, G W "Financial Questions in United States Foreign Policy" p 81

permits in such a way that no German importer could obtain delivery of goods until he had received foreign exchange permit authorising him to pay for them This meant the extension of control which had previously been exercised only in connection with certain raw materials to the whole range of German imports The British Government therefore wanted that this weapon should not be used against the British goods The first article of the Agreement provides that the German Government shall issue foreign exchange certificates without restriction in respect of the import into Germany of the United Kingdom goods of all descriptions (including in particular coal and coke for use in the German customs area), coal for use as bunkers for German and foreign ships herrings, yarns, tissues, textile manufactures The Reichsbank also undertook to devote each month for the payment of British exports to Germany 55 per cent of the value of German exports to the U K Article 4 dealt with the repayment of outstanding trade debts The German Government undertook to provide immediately a sum of not less than £400 000 for this purpose, and to provide a further sum by a credit operation or otherwise through the realisation of outstanding German commercial claims on the United Kingdom Under Article 5, the Sondermark Agreement was abrogated and arrangements were made for the liquidation within three months of existing commitments in respect of Sondermarks Should it appear that the rate of liquidation of Sondermarks was too slow to be accomplished in this space of time, the British Government reserved the right to demand their liquidation as a first charge on the foreign exchange earmarked under the first article for the payment of British exporters For the liquidation within twelve months of the balance of arrears of outstanding commercial debts not covered by the operations specified in Article 4, a further 10 per cent of the value of German exports to the United Kingdom is to be set aside provisionally for this purpose, a proportion which will be increased if necessary in order to secure the completion of the process not later than the end

normal No wonder that payments agreement have proved more satisfactory in their working[1]

The German Experience with Clearing Agreements—The German experience of clearing agreements with the creditor countries is far from encouraging The tendency of these clearing agreements to offset the mutual balance of trade between the two clearing partners tended to make Germany s balance of trade with her creditor countries unfavourable The bureaucratic working of the system has tended to restrict German trade This is so because the foreign importers of German goods prefer to make their purchases from countries where they are free from the complexities of clearing regulations Thus German exports are discouraged On the contrary the imports into Germany tend to increase due to the guarantee of payment provided under the clearing system[2] Besides the fall in German exports is to some extent due to very strict regulation of registered mark payments and the rise in the German cost and price structure No wonder, therefore, if feeling is growing that the system of clearing agreements has failed to stimulate the growth of Germany s foreign trade There is a great deal of truth in the remark of Dr Schacht that the clearing agreements are responsible for the fall in Germany's exports The German ability to pay the debts has been limited

According to some writers[3] however the system of clearing agreements has enabled Germany to maintain her supply of foreign raw materials and half finished goods sufficient to keep the great and complicated machinery of German production in full swing It is argued that Germany's less active balance of trade with a few countries

merely shows that more raw materials and half-finished goods have been imported from these countries than formerely Besides, the clearing agreements have opened up possibilities of trade with the newer raw material countries, which have shown their eagerness to buy more German goods in order to balance their clearing accounts Thus, the clearing system has opened up invaluable new trade possibilities Mr Ritter adds "I have no doubt that, in view of the existing world conditions with regard to currencies, debts credit and commercial policy German trade and industry would not have been able to reach and maintain their present momentum without the clearing agreements This favourable effect of the clearing system is not limited to Germany, the numerous countries which have been able to increase their exchange of commodities with Germany under that system have also profited from it "[1]

It is very difficult to agree completely with Mr Ritter There is some truth in his claim but it is exaggerated. For on a dispassionate consideration, it cannot be denied that the German trade and industries have suffered serious hardships during the periods of the currency of these clearing agreements The bureaucratisation of trade has proved definitely harmful. Besides, the tendency of clearing agreements towards equalisation of import and export trade between the contracting countries has increased the difficulties of creditor countries[2] To counteract these baneful tendencies, Germany has changed over to "payments" agreements since 1934.[3] Germany, it should be noted, was able to obtain the raw materials needed by her industries with great difficulty, and that, too, because under the "New Plan" the official German policy has been deliberately directed towards the increase of purchases from those countries with which Germany's trade balance is still active No doubt, due to her economic and geographical position, Germany has been able to exploit this expedient

1 Ibid, p. 472

2. Vide Harris, C. R. S., "Germany's Foreign Indebtedness," p 74.

Vide, Hamburg Bulletin, Vol. III, No 11

better than other countries, but it is idle to deny that exchange control has not restricted German trade

The German experience of clearing agreements is in no way peculiar, it is a common experience of all debtor countries The clearing agreements have generally restricted the volume of international trade The creditor countries have also felt the adverse effects of these agreements and their trade has declined Due to the disparity between the cost and price structure of countries imposing restrictive exchange control and those relatively free from it, the former group finds it more profitable to trade with the countries within the group Where the exchange control is rigidly maintained and the adjustment in exchange rates is not permitted the exchange control countries find it extremely difficult to trade with free currency countries Even between the exchange-control countries *inter se* the scope for expansion of trade is limited It is significant to note that trade between the exchange control countries has also tended to decline The export subsidies have undoubtedly rendered invaluable help in encouraging exports, but they have not been able to counteract the forces created by the restrictive measures The policy of internal deflation resorted by some countries to counteract the effects of exchange control had to be given up due to strong public opposition

Further, the clearing agreements have failed to solve the problem of surpluses and balances It will be remembered that the clearing agreements were entered into in order to tackle effectively the problem of surplus commercial claims In practice, commercial claims in arrears have tended to accumulate even after the introduction of clearing agreements Thus, the failure to secure liquidation of commercial claims in arrears, to which the clearing agreements owed its origin, contributes to their survival Restrictive commercial policy has given them a long lease of life, it has made their negotiations inevitable and continuance indefinite

Compensation Agreements—The shortage of foreign exchange and transfer difficulties are responsible for the growth of compensation agreements They are essentially barter arrangements and often of a secret character Compensation means the direct exchange of goods for goods between the contracting countries The main purpose of these agreements is to so offset imports against exports that the necessity of foreign exchange to facilitate the transaction is completely eliminated[1] Compensation agreements may be entered into between private parties without Government control or supervision or they may be agreements between private firms to be worked under State supervision, or the agreement may be entered into between States directly In the case of private compensation agreements, the procedure is to "marry" foreign trade transactions in such a way that the importer in each country, instead of making payments to the foreign exporter, pays the domestic exporter of his own country In the case of compensation arrangements worked through the Government and semi-government agencies, the government pays the suppliers in their own domestic currency. The transfer of balances is eliminated Thus compensation agreements afford a corrective to clearing agreements

Technique: German—This new technique has been developed considerably in Germany The scarcity of foreign exchange, and the 'New Plan' introduced by Dr Schacht at the end of September 1934, under which German importers are not permitted to import unless they have previously obtained foreign exchange permits to pay for them, have stimulated the conclusion of compensation agreements

The simplest form of compensation agreements is a direct barter transaction between the two contracting governments, under which, for instance, so many tons of coal are directly exchanged against so many bags of coffee, each

1 "While in the clearing system the importers have to pay the purchase price in national currency into the clearing account and the exporters of the same country receive payment from the proceeds of that clearing account, in the case of compensation no money changes hands." Vide Einzig "The Exchange Clearing System," p 192

government paying the supplier in the currency of its own country

In the case of private transactions,[1] however, though the principles is the same, its application is much more complicated Such compensation transactions may be divided into four different categories When the compensation transaction is carried out between an importer and an exporter on each side, i e, in Germany and the other country with which compensation comes into operation, it may be termed a private four-party settlement transaction If in either of the two countries exports and imports are in the same hands, it is called a three party settlement transaction If in both countries the import and export transactions are carried on by only one firm each, the transactions become, according to German foreign exchange law, barter If a compensation transaction arises between several firms in Germany and another country with which Germany has a clearing agreement, the transaction is called a reciprocity transaction The mechanism attempts to "marry" foreign trade transactions in such a way that the importers in each country, instead of making payment to the foreign exporter from whom he received the goods pays the exporter in his own country

The private compensation or barter transactions are supervised by the Foreign Exchange Control and the Import Control Offices Imports are divided into two categories, 'established imports' and 'new imports' For 'established imports' the Foreign Exchange Control Office may grant each firm a license for compensation transaction up to RM 500,000 monthly Extra licenses may also be granted and payments are usually made to the clearing-office though private barter agreements are also permitted outside the clearings with the consent of foreign central banks concerned and the Reichsbank In the case of 'new imports'

compensation transactions are only permitted on the condition that the proceeds of the German exports must exceed that of the import by at least 30 per cent., the balance in foreign exchanges to be handed over the Reichsbank. Here also the additional exports procedure may be used when the dividend accruing exceeds 30 per cent. of the value of the imports But these restrictions may be ignored when the German exports are made to those countries which have a clearing agreement with Germany, and if Import Control Office concerned is satisfied that the import in question is of great economic importance These transactions both for 'new' and 'established' imports are subject to two further conditions the German exports must be made to the country from which the import of the raw materials originated or in which the imported goods in the case of semi and completely manufactured goods, have received further treatment. The payment of any kind of premium to the exporter is also forbidden.[1]

The changes in Germany's foreign trade have deprived compensation business of its character as a promoter of exports In view of the recent developments in the German economy, foreign trade has undertaken a new task in its relation to the whole economy After the recovery from the crisis the chief stress in the foreign trade policy originally lay on the export trade, whereas in about the last quarter of the year 1935 it came to be laid on the import side[2] In the earlier stages special attention was paid to the export trade in order to provide employment to the people In 1935, the problem of covering the growing import demand became of prime importance due to the rapid increase in armaments Thus, the German exports are now expected to cover the import requirements

Out of this shift in the structure of foreign trade, there arose the necessity of strictly supervising the price-relation between imports and exports The Import Supervising Office

1 Vide Harris, C. R. S., "Germany's Foreign Indebtedness," pp. 6[illegible]

2. Vide Hamburg Bulletin, Vol. II, No. 18

is thus entrusted with the task of a strict price control The examination of prices has been supplemented by an examination of the quality of goods imported Further, as a result of this fundamental shift greater preference is shown in compensation transactions to the necessities as compared with other type of goods Hence, a number of German export goods have been excluded from the sphere of compensation The most essential imports are specified on a definite list Only the goods on this list are in principle capable of being used up to 100 per cent for purposes of compensation with German export goods On the second list appear goods for the export of which private settlements are illegal In this list are included those goods which Germany imports from foreign countries, goods which Germany exports after some finishing process which does not yield good profits, and the goods of which the export position is strong enough to enable them to be reserved in foreign trade as an important source of getting free foreign exchange The third list of goods further restricts the possibility of compensation transaction with the non-European countries with which there are no payment or settlement agreements In fact it supplements the second list with goods on the import of which the countries in question are sufficiently dependent to make the goods providers of foreign currency In respect of some of the goods on this list compensation transactions may be entered into after each individual case has been examined by the Reichs Commissioner for Foreign Exchange Goods of German origin for which more than 20 per cent of the export value has to be spent on foreign raw materials are also excluded from the scope of compensation, unless the proportion of foreign raw and auxiliary material accrues in foreign currency and this is delivered to the Reichsbank. Settlement by compensation of export goods not on the exception lists is allowed only up to one third of the export value, unless the imported goods are in the list of necessities

The list of exclusions is being gradually extended due to changes in the German economic requirements Compen-

price disadvantages for German imports connected with compensation traffic In this way the danger of price disparities between the prices for German imports and exports will be eliminated [1]

From the foregoing review it will be seen that the compensation mechanism, which was developed to make up some of the deficiencies of the clearing system, has created its own problems Albeit the compensation system is more effective in maintaining volume of international trade, in face of an artificial rate of exchange than the clearing arrangements, it tends to restrict trade The protracted and complicated negotiations involved in formulating a compensation agreement, the bureaucratic and cumbersome procedure, the complicated arrangements for compensation in the case of unsatisfactory shipment and non-payment by one of the parties, and, finally, the considerable variations between dates of payments, which arise from the fact that the purchase price for exported machinery may be due in six months time, while imoorted material must be paid for in cash, are all circumstances which add to the risks and difficulties of this type of trading [2]

General Effects of Clearing Agreements—The system of clearing agreements automatically tends to extend its scope and domain Once a country resorts to clearing agreements it should have a network of such agreements to prevent artificial transit, as the German experience proves, if it is to reap the advantages incidental to such an arrangement Being essentially obligatory and bilateral in their character, the clearing agreements tend to divert the trade of a debtor country towards the creditor country which is a party to the agreement to the prejudice of third countries [3] Further, the ability of the debtor country, with weak

the future The answer is two-fold The moderate type of exchange control with suitable modifications is certain to remain as a normal part of our monetary mechanism[1] even after the desired currency stabilisation has been achieved The reasons for this change are obvious 'Even if the gold standard is restored in most countries within the next few years, it will not be allowed to function automatically but will be supplemented by intervention whenever necessary'[2] The chances of automatic maintenance of stable exchange rates are expected to be much smaller than before the war The reasons are that political debts are increasing, exports of capital are more political and psychological rather than economic, the floating balances have increased and their migration is more frequent, the growing trade restrictions make international adjustments more difficult, the exchange speculation has grown and become international, the tendency to hoard gold reduces liquidity when it is most needed, and the credit policy pursued is extremely short-sighted All these tendencies have conspired to complicate the monetary problem The result is that in future either exchange rates will have to be flexible or control of the foreign exchange market will have to be more active Further, even with flexible exchange rates some control by the monetary authorities will have to be exercised to prevent excessive exchange fluctuations

The rationing type of exchange control however, will have to be gradually given up The public opinion is gathering strength against the rigidity uncertainty[3] and waste inherent in the system which the governments cannot long ignore They tend to increase domestic costs and

prices, discourage imports and restrict exports The dislocation and instability of trade impairs its full potential value, even if the aggregate physical volume remains the same The system of blocked accounts will have to be abolished at the earliest opportunity[1] Thereafter the clearing system, which has been regarded as only a makeshift involving a number of drawbacks, will have to be abolished The essential prerequisites for the abolition of the system are in the main three (1) permanent arrangement for settling the problems of foreign indebtedness and their scaling down to suit the ability to pay, (2) adaptation of exchange rates to the relative cost levels, (3) and a reduction of trade barriers International liquidity needs to be increased The danger is that if these makeshift arrangements are permitted to remain in force for some years more, without prompt and effective checks, the new distorted channels of trade will become permanent

Signs of a change for the better are not lacking The volume of foreign exchange reserves has been reduced and their location is relatively more stable Thus the dangers incidental to their more frequent transfers have been eliminated. The total volume of short-term international indebtedness has been reduced, which augurs well for the the future The rise in the value and size of monetary gold stocks has improved the liquidity and added to the ability of the system to withstand shocks Therefore, there is no need to despair At the same time delay in taking effective measures is apt to cause irreparable damage to the economic system

1 "In present circumstances it seems that the continuance of exchange control systems and of 'Clearings' constitutes one of the most serious obstacles to the development of international trade" Vide M Paul Van Zeeland.

The *Conclusions* may now be summarised:

(1) Some form of moderate exchange control will have to be maintained even after currency stabilisation is achieved This would minimise the risk and uncertainty resulting from the sudden flight of capital

(2) The rationing type of exchange control must be immediately relaxed and gradually abandoned, if the world trade is to be revived

(3) The rigidity of clearing agreements may be relaxed by making the exchange rate agreed to therein approximate to the market rate

(4) The currencies should be stabilised so as to remove the disparity between the internal and world price levels and establish an equilibrium

CHAPTER VI

THE MOST-FAVOURED-NATION CLAUSE

FROM what has been noted in the preceding pages it will be seen that the technique of commercial policy has recorded remarkable changes since the inception of the depression in 1929 The result is that the structure of commercial treaties has had to be moulded to suit the changed economic conditions[1] The quotas various forms of exchange control widened scope of Imperial Preference, subsidies, marketing arrangements, etc, have deprived tariffs of their former glory and relegated them to the background The importance of the Most Favoured Nation Clause in the structure of modern commercial treaties has not remained unaffected from these important developments In the present chapter therefore, an attempt will be made to study the part played by the M F N Clause in the structure of modern commercial treaties

Bilateralism.—In view of the dislocations and disturbances in international economic relations described in the foregoing chapters, trade agreements entered into by different countries are tending to be increasingly exclusive Rigid bilateral trade agreements are resorted to in order to find export markets, which are being closed as a result of growing restrictions on international trade In these rigid bilateral trade agreements, quotas, clearings, compensation, barter, and payments arrangements play a more important part, which tend to restrict, rather than revive,

international trade by deflecting it in artificial and uneconomic channels[1]

Further these bilateral treaties have been largely temporary compromises of short duration, intended to keep the hands of the contracting countries free to adjust their commercial policy to suit national requirements Throughout this period the world economic policy has been erratic and increasingly restrictionist In these days of shrinking foreign trade each country has tried its utmost to divert the channels of trade, to suit its immediate interests, by novel expedients, refraining at the same time from any permanent commitments The uncertainty inherent in such arrangements increases risks and ultimately restricts trade

The restrictive effects of this artificial diversion of trade from its normal channels is apt to put severe strain upon the economic systems of the third countries, from which even the countries imposing these restrictions can hardly escape The bilateral balancing of trade has become almost universal and increased the fetters on international trade[2] Discrimination is implicit in a policy of substantive bilateralism That discrimination has dangerous consequences is accepted It is not a new problem, it arose with the growth of modern industry and commerce To combat its baneful effects, the M F N Clause was devised and has had creditable results

Discrimination.—A discriminatory trade policy acts as a strong check to the optimum utilisation of world's economic resources It distorts the channels of trade and increases the risks thereof Production for export markets

become hazardous and the industrial efficiency receives a setback. Discrimination is injurious both to the country following such a policy as well as the countries against which the discrimination is practised.

Equalising Conditions of Competition.—Measures calculated to equalise the conditions of competition between different countries do not savour of discrimination. According to international commercial practice it is conceded that every nation has a right to levy a reasonable tariff on goods imported from abroad. What should be the absolute incidence of these duties or other protective measures is purely a domestic question of the country concerned. The national sentiment must be given reasonable scope for free play, for the road to internationalism lies through healthy nationalism. Although the height of the protective tariff and the nature of other protective measures are to be ultimately determined by the countries concerned, it is agreed that these measures ought to be limited by the principle of equalising conditions of competition. Therefore in practice the basic principle of all protective legislation is to resort to only such protective measures as will equalise the differences between the costs of production at home and abroad and, at the same time permit reasonable profit to national industries. The principle of equalising conditions of competition with a fair margin, however does not provide that all industries should indiscriminately be protected. The national welfare should be the guiding principle of protectionist policy. So long as these protective measures are reasonable, permit only fair profits to essential national industries under efficient and honest management and are uniformly enforced against all foreign countries there is no discrimination or preference, and international amity prevails.

Thus, although the protective measures are purely a national concern, the salutory limitation is that they should be reasonable and just sufficient to equalise the conditions of competition with a fair margin of profits, and nothing more. The industries protected must add to the national

welfare Therefore the protective measures which do not fulfil these conditions are apt to strain the international economic relations and lead to retaliation and tariff wars The Hawley-Smoot tariff and its repercussions are an illustration in the point [1] Therefore in some of the more important countries the usual practice is to allow the foreign commercial interests to put their case before the Tariff Commission when it is examining the claims of any domestic industry for protection Of course the foreign interests have no right to be heard it is only as a matter of courtesy that they are given a hearing [2] This step is taken to remove misunderstanding Thereafter the Tariff Commission makes its recommendations to the Government The protectionist policy therefore if it is to remain a purely domestic concern of the country pursuing it must be very carefully and cautiously determined, and the foreign interests affected thereby given due consideration.

From the foregoing discussion it follows that protectionist measures, even though uniformly enforced against all countries may result in international friction if they are unfair and go beyond equalising the conditions of competition In such cases they must be a subject of international discussion and negotiation When however, the measures are obviously preferential and discriminatory they cause conflict The plausible arguments in favour of special reciprocity treaties and preferences do not alter the hard fact that a nation discriminated against has a grievance which it may nurse into a hatred History of American tariff policy shows the futility of exclusive commercial bargaining from the national as well as international standpoint It records the triumph of sectional vested interests over the national welfare

Equality of Treatment—For the smooth functioning of the international economic mechanism it is essential that discrimination and preferential treatment in commercial practice should be given up Individual countries can make

distinct contribution in this direction by keeping their protectionist policy within reasonable limits and extending equality of treatment to others Just as each nation claims a right of protecting itself against discrimination it should recognise its obligations of extending equal treatment to other nations The Most Favoured Nation Clause is a very useful instrument to achieve this end It is intended to provide for equality of treatment In general the essential purpose of the Clause in a commercial treaty with another country is to provide a guarantee that the goods exported by the contracting country shall be treated on a footing of equality with those of any other foreign country The Clause therefore provides a guarantee against discrimination an equality of treatment It does not concern itself with equalising the conditions of competition between different countries Similarly the Clause is not necessarily associated with any particular type of commercial policy

Nature of the Most Favoured Nation Clause—The equality of treatment which the M F N Clause attempts to accord may be (1) conditional or unconditional (2) limited or unlimited (3) reciprocal or non reciprocal The promise is conditional when the contracting parties mutually agree to extend any particular favour in respect of commerce and navigation granted to another country immediately to the other party freely if the concession was freely made or in return for a compensation as nearly as possible of proportionate value and effect to be adjusted by mutual agreement if the concession was obtained at a price Under the unconditional pledge the contracting parties agree to give immediately and without compensation to the other party every favour which one of the parties has actually granted or may hereafter grant to a third power The pledge may be limited only to particular categories of goods When the pledge is unlimited it applies to every favour privilege or immunity In the case of reciprocal promise both the parties agree to extend mutually the favours, privileges and immunities already granted or to be

granted to a third power Here each party to the contract has both a right and an obligation But when the promise is non reciprocal only one party to the contract undertakes to extend to the other party any favour granted to a third state the other party has no obligations Such one sided treaties are concluded between strong and weak states For instance the Anglo Siamese Treaty of 1855 was non reciprocal It provides The British Government and its subjects will be allowed free and equal participation in any privileges that may have been or may hereafter be granted by the Siamese Government to the Government or subjects of any other nation'[1] Similar non reciprocal obligation was imposed upon Germany under the Treaty of Versailles

From the foregoing it will be seen that the unconditional unlimited and reciprocal M F N pledge is most effective in eliminating entirely the evil of discrimination in commercial policy According to this form of the Clause every contracting party is vested with a right to claim immediately as of right and without compensation all commercial favours privileges and immunities accorded to the nation most favoured whether such concessions result from autonomous action or from conventions concluded with third countries Other forms of the Clause savour of discrimination and do not accord equality of treatment which is essential and invaluable for smooth *functioning of the international economic system*

The Conditional M F N Clause—Of these several interpretations of the M F N Clause there has been considerable controversy on the conditional and unconditional forms As adverted to above the conditional form of the M F N Clause creates an obligation on the contracting parties to extend every favour privilege or immunity in matters of commerce and navigation extended to a third state to the other party, but the obligation is qualified by the most important condition that if the concession to the third state was granted in exchange for an equivalent, it

will be extended under the treaty only for an equivalent Thus the conditional form makes a distinction between concessions gratuitously made and the concessions made in return for an equivalent and provides that a favour granted to a third nation for a compensation does not create in the technical sense a 'favoured nation with the result that the other party to the trade agreement cannot claim the advantages of the concession without offering an equivalent concession [1] In principle this interpretation of the Clause also intends to secure equality of treatment and perhaps a more equitable one In practice however, as an instrument of commercial policy it fails to remove discrimination

Defects of the Conditional M F N Clause—It is essential at this stage to have a brief review of the disadvantages and inadequacy of the conditional form of the M F N Clause The most serious practical difficulty in the application of the conditional form of the M F N Clause is the determination of what constitutes an equivalent concession [2] It is very difficult to assess precisely the value of the different concessions which the parties may be prepared to offer The parties concerned many have different tariff systems and their interest in concessions is apt to vary so that it would be difficult to have an agreed valuation Besides several concessions are often simultaneously made

by the parties in a single commercial treaty, so that it is impossible to say what has been paid for each concession [1]

Further, it would lead to tremendous waste of time and effort, since under this system each commercial treaty to be negotiated would involve a consideration of all concessions granted in previous treaties together with those proposed in the new agreement [2] past as well as future Besides, there is a possibility that each one of the new bilateral agreements negotiated under the conditional M F N Clause may affect the concessions accorded to other countries in the past in similar commercial agreements To remove this new discrimination the old treaties would have to be revised In the meantime, the enforcement of the new trade agreement would create commercial discrimination, which the revision of old pacts may remove Dr Gregory rightly remarks that the conditional M F N Clause presents a serious obstacle to the conclusion of tariff treaties as soon as the commercial relations between States become complex, because of the difficulty of re-bargaining the whole of the concessions on the conclusion of each successive treaty [3] However elaborate and efficient the machinery for the negotiation of trade agreements may be discrimination under the conditional form of the M F N Clause is difficult to eliminate,[4] it breeds discrimination [5]

The differentiation in customs treatment, consequent upon the enforcement of the conditional M F N Clause would complicate the technique of commercial policy and add to the administrative difficulties Under such circumstances, international trade is apt to shrink The remarkable decline in multilateral international trade recorded during recent years is due, *inter alia*, to exclusive

bilateral commercial treaties The conditional[1] M F. N Clause would have similar restrictive effects Mr Grady rightly remarks "The conditional most-favoured-nation principle has inevitably degenerated into a vast and complicated system of bilateral arrangements which have made international commerce in effect commercial warfare, with countries forced to buy from each other which are not, in a true sense trade building concessions, but rather tribute for immunity from acts of commercial aggression "[2]

Again, a country cannot incorporate conditional Clause in some of its commercial treaties and unconditional in others The existence of a single unconditional most-favoured-nation pledge in a country's commercial treaty makes all the other pledges, whatever their form, unconditional in effect[3] Therefore a country anxious to pursue an effective conditional policy must do so in respect of all its commercial treaties, it needs to be a general policy permitting no exception The universal adoption of the conditional M F N Clause in commercial agreements amounts to complete abandonment of the most-favoured nation treatment This is so because under the conditional M F N Clause a country has to purchase each concession at a price acceptable to the other party, which, in effect, amounts to having no treaty rights at all Thus the conditional M F N Clause contained in a commercial treaty, in practice, neither imposes any obligation on the country granting it nor confers any valuable right on the country

receiving it, it is a meaningless pledge[1] In short, the conditional M F N Clause perpetuates commercial discrimination it was expected to remove[2] It imports needless complications in the technique of commercial policy, leads to commercial insecurity, and restricts international trade

Conditional American Practice—Notwithstanding these defects, the conditional M F N Clause was consistently adhered to by the United States throughout the pre-war period It was in 1922 under Fordney-McCumber Act, that this traditional policy was abandoned On a closer study of the American economic history one finds that practice of the conditional M F N Clause was not so illogical as it might appear at first sight The bargaining power of a country exporting agricultural products is greater as compared with that of an exporter of manufactured goods, and the structure of its industries is less vulnerable to retaliation,[3] since its exports constitute the primary raw materials of manufacturing industries Normally, the imports of raw materials are not lightly penalised Therefore, the United States could follow conditional practice with very slight damage to her economic structure From the advanced industrialised countries, who were offering unconditional M F N treatment, the United States received,, by virtue of her conditional M F N treaties everything which she could have received if they had all been unconditional In return she gave nothing Whenever she made any concessions for compensation to any

country they were extended to third states on the basis of strict bargains Thus, the United States acquired all the advantages of the unconditional M F N practice without any sacrifice

America Discards Conditional Practice.—The shift in American policy, from the conditional to the unconditional practice during the post-war period was due to changes in the structure of American industries and the international economic relations The dependence of American industries on foreign export markets had increased which made them more vulnerable to discrimination The American manufacturers therefore could not afford to continue with their traditional indifference towards other countries Besides, the American agricultural exports were also faced with increasing competition from other agricultural exporting countries in the export markets To this must be added the growing trend towards agricultural protectionism in industrialised countries In view of all these changes, the United States had to adopt a more responsive attitude towards other countries Again, the American tariff schedules had become more complex, which increased the difficulties of commercial negotiation under the conditional M F N Clause "If the problem of determining a *quid pro quo* necessitated by the conditional Clause was difficult before the World War, it now appeared well nigh insuperable"[1] Further, in the early post-war years discrimination had become more rampant in European countries, which neutralised the advantages accruing to the United States from the conditional practice, she could no longer expect to obtain the benefits of tariff concessions accorded in commercial treaties by foreign countries through generalisation Thus, what the Americans needed more earnestly than ever, under the aforesaid circumstances, was the equality of treatment through the unconditional practice

Nature of the Unconditional M F.N. Clause—From the foregoing analysis it is clear that discrimination is

1 Vide Dr Tasca "The Reciprocal Trade Policy of the United States," p 118

inevitable under the conditional practice, it fails to guarantee equality of treatment The only other alternative is the unconditional M F N Clause[1] which generalises simultaneously and unconditionally without request and without compensation the advantages granted by either contracting party to the third states The outstanding advantage of the unconditional M F N Clause over its rival is that it guarantees complete equality of treatment So also it helps to reduce undesirable interference of the State with trends of international trade Above all it eliminates waste involved in determining the *quid pro quo* while negotiating commercial treaties The unconditional Clause is more in keeping with the needs of a progressive community It enables more effective utilisation of economic resources than would be feasible under the conditional Clause

Since the evolution of modern industry and commerce, the unconditional M F N Clause has played an important part in the negotiation of commercial treaties Except in few cases most of the modern trade agreements incorporate the unconditional Clause It was popular during the period of industrial and commercial expansion With the setting in of the depression however it became either unpopular or was completely discarded as an instrument of commercial policy Thus between 1860 and 1914 a period of rising commercial and industrial activity use of the

Clause was more common, in fact, it had become 'the golden rule' of commercial policy Similarly during the period of recovery which followed the early post-war depression, the Clause regained its popularity and was incorporated in important commercial agreements With the inception of the Great Depression in 1929, the Clause has once again received a serious setback from which it has not been able to recover, its future is in danger.

The expansion of world trade and industries, to which popularity of the unconditional Clause may be traced. was due to the existence of three fundamental conditions[1] (1) freedom to trade in goods without quantitative limitations, although subject to customs duties, (2) unhampered convertability of currencies in the international market, (3) currency stability in such a degree as to preclude sudden disturbances of the competitive bases and to allow at any rate approximate estimates of profit and loss to be made Thus, stable economic system, an international monetary mechanism and relatively moderate restrictions on trade are essential pre-requisites of the unconditional practice. This is so because under stable economic conditions manufacturers and producers demand for their exports no more than equality of treatment in foreign markets To have the equality of treatment for its exports each country will be willing to accord similar treatment to the products of other countries in its own market In short, the unconditional Clause would be effective only so long as the normal mechanism of international trade functions

With the breakdown of the machinery of trade, the Clause is bound to lose a great part of its effectiveness This break comes with shrinkage of foreign trade, collapse of international monetary mechanism and distortion of the channels of trade by an extreme protectionist policy The stages in the development of the world catastrophe are relatively well-marked The moment optimism, characteristic of expanding trade and industries, receives a check several industrial undertakings find themselves

1 Vide "The Most Favoured-Nation Clause," (League of Nations) 1936.

involved and huge losses are incurred This marks the downward swing of the trade cycle During the period of recession and shrinking trade the national attention is centered on the home market and a complicated technique of protection is evolved to make the country self-sufficient [1] In the export markets the equality of treatment is thrown overboard and exclusive concessions are sought Discrimination becomes rampant

The sudden and steep collapse in prices puts out of gear the international monetary mechanism This leads to devaluation, foreign exchange control, etc, and the trade records further recession The defensive measures of the extreme type thwart their purpose, for they distort the channels of trade Under such circumstances it is no longer possible for the unconditional M F N Clause to guarantee equality of treatment

The world economic tendencies since the inception of the present depression in 1929 have upset the economic equilibrium and distorted the channels of trade The growing economic nationalism and the complex technique of protection, which came in vogue to preserve the remnants of trade, have had far-reaching restrictive effects With the strangling of international trade, the advantages afforded by the unconditional *M F N Clause* have diminished and its limitations magnified [2] Therefore we now propose to study in detail the effects of these new developments in commercial policy on the working of the Clause

Non-Tariff Restrictions on Trade—Before we take up *the discussion of these new forms of trade restrictions,* particularly the quantitative trade restrictions, it is necessary to answer the question as to whether they fall within the scope of the M F N Clause. General opinion on this question is divided It is argued that

these restrictions do not *fall* within the scope of the Clause because it is impossible to attain equality of treatment with them.[1] This narrow interpretation is however, challenged by some eminent economists They argue that all trade barriers—tariff and the non-tariff—are within the scope of the Clause[2] It is not desirable to put a narrow interpretation on the Clause and restrict its scope only to tariff barriers No doubt in the past the Clause was applied largely to tariffs, it was so because other restrictions did not exist The inference that these restrictions were excluded from the scope of the Clause is not warranted The usual form of the Clause includes an undertaking to extend to the other contracting party every favour, privilege or immunity accorded to the third State[3] These terms are sufficiently wide to include every form of trade restrictions From the fact that tariffs alone were specified, it is not correct to argue that other forms of trade restrictions were excluded The exclusion, to be enforceable, must be expressed in the treaty Besides, the Clause is intended to prevent discrimination, and secure equality of treatment In so far as non-tariff restrictions lead to discrimination, the Clause is intended to check them Where the M F N Clause has been liberally interpreted it has minimised considerably the discrimination under the quotas,[4] rationing form of exchange control,[5] etc Of course, in the case of tariff restrictions the Clause has had a marked success in

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1 "We have seen that the quota stands in opposition to the Most Favoured Nation Clause because the global quota favours neighbouring countries while a geographical division based on imports in certain years favours countries which happened to send large quantities during those years. Thus it must involve some discrimination which is contrary to the terms of the Clause This Clause which rests upon the principle of equality of treatment loses its significance when quotas are introduced." Vide Haight F A. "French Import Quotas," p 93.

2. Vide Prof Rist The Improvement of Commercial Relations between Nations and the *Problem of Monetary Stabilisation*, 1936 p 120

3 A few illustrations may be noted. The Cobden Treaty (Anglo-French) of 1860 lays down

"Each of the two high contracting parties binds itself to give to the other party every favour every privilege or decrease in import duties on the articles mentioned in the present treaty which one of the parties may grant to a third power

The Treaty between U K and Austria—Hungary of 1876 provides as follows:

"Every reduction in the tariff of import and export duties as well as every favour or *immunity* that *one of the contracting parties grants to the subjects and commerce of a third* power shall be participated in simultaneously and unconditionally by the other"

Such instances can be multiplied. Vide Dr Gregory T E.: "Tariffs" p 451

4 See Chapter IV

5 See Chapter V

eliminating discrimination and according equality of treatment to the contracting parties Its success in checking discrimination incidental to the non-tariff restrictions has been much less marked Part of the failure is due to the faulty administration of these non-tariff restrictions, which can be considerably improved, given a sincere desire on the part of the parties to do so If in spite of mutual co-operation the Clause does not succeed in according as complete an equality under the non-tariff restrictions as it did in the case of the tariffs, the defect is to be traced not in the Clause but in these new devices which should be suitably modified No doubt the new impediments to trade have weakened the effectiveness of the Clause, but that strengthens the case for a more liberal and universal use of the Clause, rather than against it Even under the new regime, the Clause provides relatively much better equality of treatment[1] than would be had without it So far as the tariff barriers are concerned, which are even today much higher than they were ever before[2] the Clause provides eqality of treatment In short, the Clause, if liberally interpreted, includes within its scope both tariff and non-tariff restrictions on trade

Major obstacles to the Operation of the M. F. N. Clause :—

The Quota System—The quotas constitute a more serious obstacle to the proper functioning of the unconditional M F N Clause Their discriminatory administration neutralises the equality of treatment Wherever they have been placed within the scope of the Clause, their discriminatory effect has been considerably weakened by the incorporation of the Clause in the treaties containing quota provisions

The quotas, hitherto tried, have been of three types (i) arithmetical or equal quotas, (ii) global or unallocated quotas, and (iii) proportional quotas Under arithmetical system each country is accorded an equal quantum of a

commodity to be imported This type discriminates in favour of the relatively backward countries and against the more adavnced[1] ones Therefore the commercial treaties containing the unconditional Clause do not make use of this form of quotas The discouragement of this type of quota arrangement has been beneficial to the country imposing quotas in particular and the world in general Where this form has been, or is being used, it amounts to complete negation of the unconditioral Clause

Under the global quota system the country resorting to such an arrangement fixes the total quantity of commodity to be imported, and permits all countries to compete unfettered for the market This method is obviously equitable and in accord with the principle of equality of treatment, but it presents considerable practical and administrative difficulties Its use, therefore has been extremely rare

The proportional method has been found most practicable and at the same time more in keeping with the spirit of the unconditional Clause Under this system a basic period is selected, and each country is allowed to import a definite proportion of the total quantity imported during the basic period But, considerable difficulties are encountered in selecting the agreeable base period and fixing the quotas Besides in view of the rapid changes to which the structure of modern industry is subject, the statistics of the past may not correctly indicate the current requirements and therefore provide a most unsatisfactory base for the most sensitive and delicate mechanism of international trade to rest upon It must lead to a static condition in international trade This method, however, provides theoretically the most equitable treatment possible under the quota arrangements

1 "This method tends to give artificial encouragement to imports from countries which export little and where costs of production are high to the detriment of countries that enjoy natural advantages and economic conditions favourable to exportation." Vide The Most Favoured Nation Clause" (League of Nations) 1936

From the foregoing it will be seen that the quota system endangers equality of treatment and thereby weakens the effectiveness of the unconditional Clause But the fault does not lie with the Clause The changes in the international economic relations explain the present predicament On the other hand, the Clause has increased the popularity of the proportional quota system which provides equality of treatment to the maximum degree feasible under the quota system

The Refinement of Tariff Classification—The growing refinement of tariff classification has also adversely affected the equality of treatment, which the unconditional M F N. Clause seeks to secure in international trade Minute distinctions are introduced in tariff schedules so that third parties may not be able to secure benefit of tariff concessions under the most-favoured-nation treatment accorded in bilateral commercial treaties Mr Bailey rightly says "The difficulty of defining 'similarity' or 'likeness' has been seized upon as an instrument in tariff-legislation for inserting minute distinctions in tariff schedules which may be used in practice for circumventing the automatic extension to third states of concessions granted in bilateral commercial treaties"[1] This power has been frequently used to neutralise the efficacy of the most-favoured-nation treatment

Foreign Exchange Control—Under the system of exchange control all trade and capital movements are subjected to strict state supervision In the rationing type of exchange control, the state allocates foreign exchange to different varieties of imports as it thinks fit[2] Such an arrangement neutralises the equality of treatment much more effectively than the quota system The shortage of

foreign exchange necessitates discrimination between goods and that leads to discrimination between countries in an attempt to adjust balance of payments

Clearing and Compensation Agreements.—The clearing and compensation agreements are essentially barter arrangements The clearing agreements provide for exclusive favours to the contracting parties distort the channels of trade and cause serious damage to the trade of third countries Discrimination becomes common in commercial practice

From the foregoing analysis it will be seen that under the modern technique of protection equality of treatment has become ineffective in commercial practice This is due to new developments in international economic system which have made the environment uncongenial for proper functioning of the unconditional Clause As adverted to above the Clause requires monetary stability free functioning of currency and exchange, free circulation of goods, and expanding triangular trade so as to be able to eliminate discrimination and provide equality of treatment The present world economic system with shrinking international trade international monetary mechanism broken down, substantive bilateralism in vogue is incompatible with the spirit of the Clause[1]

Exceptions to the M F N Clause—It is open to the parties entering into a commercial treaty containing the unconditional Clause to insert explicit exceptions The Clause as stated above intends to provide for equality of treatment Absolute equality of treatment is an ideal difficult to achieve The practical problem is to secure maximum degree of equality under given circumstances. The Economic Committee of the League of Nations held that "most favoured-nation treatment even in its unrestricted interpretation cannot be made applicable to certain

1 "Its successful life as a regulating instrument depends, therefore upon a sense of political security on the absence of undue disturbance of the financial fiscal and technical background of international trade and on the realisation of a relatively high level of international morality None of these conditions have been generally realised in the post war period." Vide Bailey S. H. "Economica" (1933) p 43"

The three Scandinavian countries, Denmark, Sweden and Norway, have traditionally followed the policy, in their commercial treaties with third states, of excluding from the operation of the M F N Clause all benefits which they mutually accord to one another The Baltic States, Finland, Esthonia, Latvia and Lithuania, follow the same practice Latvia further excludes the concessions she concedes to the U S S R The U S S R in most of her commercial treaties, excludes from the scope of the M F N Clause the privileges and facilities granted to the countries which at an earlier date formed part of the Russian Empire (i e, Finland, Esthonia, Latvia, Lithuania and Poland) and to the adjacent states on the Asiatic continent (i e, China, Mongolia, Afghanistan, Persia and Turkey)

Spain and Portugal, on the Iberian Peninsula, exclude trade with their former colonies from the scope of the Clause, in addition to the concessions mutually granted Thus, Spain in her commercial treaties excluded the special favours granted to Latin American Republics The United States, France, United Kingdom, the South American Republics, the Central American Republics, Turkey, Bulgaria, incorporate in their commercial treaties similar exclusions from the M F N Clause

These regional exceptions weaken the effect of the M F N Clause The Economic Committee of the League of Nations refrained from investigating these colonial preferential arrangements in view of their political implications But these issues will have to be faced and solved if the international economic relations are to be provided with a sound and stable basis The political struggle for imperialist expansion is one of the most important causes of the present debacle This form of discrimination therefore needs a prompt and effective check[1] No doubt in the

present atmosphere, surcharged with mutual suspicion, it will be difficult to have a common understanding, but the recent political and economic developments must prove an eye-opener to those who want to stick to the discriminatory practice on the plea that they are traditional The advanced states,[1] saturated with political and economic imperialism, will have to give up their narrow self-interest and tackle the problem with courage, firmness and foresight if the world is to be saved the spectre of tottering civilisation

(iv) **Sanitary Exceptions.**—These are exclusions based on sanitary grounds or on grounds of internal safety These exceptions are desirable in the interests of the people Thus, exclusions arising from exceptional circumstances as regards munitions of war, or for reasons of the interior safety of the State, or for reasons of sanitary policy, for the prevention of the spread of epidemics, etc, have been accepted without demur During the post-war period, however, these restrictions or prohibitions have not been confined to a special emergency of a non-economic character, but have been frequently used for protective purposes and rendered the Most-Favoured-Nation Clause inoperative

(v) **Exceptions for National Fisheries and Coasting Trade**—These exceptions[2] have also been accepted and there has been no complaint against them

(vi) In some cases the M F N treatment is accorded only to goods directly imported,[3] those indirectly imported being excluded The possibility of nationalisation is denied

(vii) **Anti-dumping Measures Excepted**—Another important exception is the imposition of countervailing duties on bounty-fed articles The complicated system of subsidies developed in recent years on a huge scale to stimulate exports, is a serious menace to the equality of treatment Therefore, the anti-dumping clause is usually incorporated in modern commercial treaties For instance, the Franco-Canadian trade agreement of 12th May 1933, excludes "measures directed against all forms of dumping provided that they are applied in the same degree and under the same conditions to all other foreign countries in regard to which like causes arise [1]

(viii) **Multilateral Conventions to form an Exception**—Since the depression, multilateral conventions have been suggested as an important potential exception to the M F N treatment [2] These conventions are discriminatory in effect But the sponsors of the conventions argue that in the present state of affairs they offer the most convenient and effective instrument for lowering down trade barriers [3] Such agreements are open to accession by all countries prepared to conform with the obligations This is their distinctive feature which separates them from other devices used for obtaining exclusive concessions Besides, they provide for the granting of the stipulated privileges to non-signatory countries which accord equivalent advantages, whether by treaty or by virtue of their own autonomous policy It should, however, be noted that the dangers inherent in such a discriminatory practice could only be avoided if such agreements were to initiate a movement for the reduction of tariff barriers generally If thus worked, the multilateral conventions will be using

discrimination essentially temporary, to combat the modern large scale and more serious discrimination in the form of imperial preference This exception should receive universal recognition, under the abnormal conditions of the present day, as an instrument for securing the equality of treatment [1]

Arguments against the Unconditional M F. N. Clause.— The dissatisfaction with the unconditional M F N Clause had been felt even in the pre-war period, but it gathered momentum during the war and in the early post-war period The unconditional practice was, therefore, discarded during these intervals But the unpopularity of the unconditional Clause was essentially short-lived Soon the practice of equality of treatment was re-established and in greater glory due to the support of the United States Germany and Great Britain also rendered invaluable help in restoring the new system With the setting in of the depression, however and the evolution of new technique of protection, the equality of treatment has been endangered once again and serious misgivings have arisen about the the utility of the Clause under the present abnormal conditions These objections may be noted, for they would enable us to assess the permanent value of the Clause and the part it can play in the economic system of the future

(i) It is argued that the most-favoured-nation system tends to promote free trade and thereby prevents young and undeveloped countries from protecting their home markets adequately Since the tariff reductions are extended under the Clause to all countries, the result is a gradual decrease in the protection accorded to the national economy This is not a correct view The

equality of treatment, which the Clause intends to promote, does not necessarily mean free trade, it means elimination of discrimination Therefore protection is consistent with the spirit of the Clause, provided it is reasonable, as adverted to above Again the Clause does not obstruct protection to the home market, provided it is reasonable and no discrimination is made between different suppliers As has been shown in the first chapter, most of the advanced countries have had to resort to protection for improving their technique of production since the early stages of industrial evolution and the most favoured nation treatment has never stood in their way The Clause penalises discrimination, and not reasonable protection determined by the domestic economic requirements Adequate protection can be provided to the home market without resorting to discrimination[1] and the wastes inherents in it

(ii) Another important objection raised against the Clause is that, instead of tending to lessen the barriers to international trade it tends to add to them The reasons advanced in support of this contention are as follows

(a) A country which would be prepared to grant tariff concessions to another will hesitate to do so if they are automatically extended to all countries To this it may be said that *it is in the interest of* the importing country itself to generalise its concessions

(b) Another argument advanced is that the value of concessions granted to a country is reduced since they have to be extended automatically to other countries No doubt the value of concessions obtained under the Clause are not exclusive, but, this fact is known to both the parties at the time they enter into the treaty, so that the question

of their subsequent lessening in value, if any, is not unexpected Besides, the mere fact that a concession is to be generalised does not reduce its value because the parties have made full allowance for this contingency in the treaty The generalisation of concessions, under the system of equality of treatment, helps all the countries Exclusive concessions result in discrimination and lead to retaliation, international ill-will and suspicion

(c) A more plausible objection is that a country will refrain from granting tariff reductions in order to obtain others in exchange when it knows that if it only waits it will obtain the benefit of the reductions that will be granted to third countries No doubt a country will gain from the generalisation of concessions contained in commercial treaties with individual countries and therefore may be reluctant to take initiative But this passive attitude is short-sighted because in the first place advantages derived from the generalisation of concessions are secondary, and secondly such an adamant attitude will cause ill-feeling In the long run, therefore, no country will find it profitable to resort to such a policy

(d) Further, it is argued that a country will not derive from a concession it is prepared to make, all the advantages the concession might secure for it, because, while granted to a contracting country in return for compensation, the concession will be extended gratuitously to all countries that refuse to "pay" to get it The concessions generalised under the Clause are not gratuitous, as they may at first sight seem The concessions, thus availed of, are usually paid for In rare cases, where a country refuses to pay it should be excluded, instead of the whole system being overthrown

(iii) Another important objection is that the M F N principle is particularly ill-suited for dealing with countries having prohibitively high single-schedule tariffs, who rely on their M F N treaties to bring them all the concessions which other countries engage reciprocally to grant to each other, but are under no real pressure to make

any concessions in return As adverted to above, the M F N treatment permits only a reasonable protectionist tariff, essentially temporary, so that a country resorting to prohibitory single-schedule tariffs could be excluded from the benefits of the Clause Such an exclusion would be an effective weapon to bring round the recalcitrant country

(iv) It is said that the Clause hinders effective tariff bargaining It prevents the negotiators from obtaining advantages through the possibility of discrimination, and from using the same concessions several times over for different negotiations, in order to derive maximum possible advantages from the successive negotiations To this objection it may be said that commercial bargaining, in the absence of the M F N Clause, would be highly complicated, it would lead to discrimination and distort the normal channels of trade It would lead to anarchy in international commercial policy Therefore, the most effective remedy is to popularise use of the M F N Clause in commercial bargaining and make it universal,[1] for any damage to the Clause would mean discrimination

(v) Another argument is that the increasing tendency towards specialisation of tariffs tends to deprive the M F. N Clause of its significance, since concessions can then be granted in such terms as to make them inapplicable to the products of third countries This is veiled discrimination and does not involve legal violation of the Clause The use of such veiled discrimination has become more marked since the depression This form of abuse can be remedied by adding a suitable pledge to the Clause to the effect that customs tariffs should not be used as a means

of discrimination against the trade of other party[1] The obedience to the Clause should be demanded not merely in letter but in spirit

The Future of the Most-Favoured-Nation Clause.—It will be seen from the foregoing discussion that the unconditional M F N Clause stands for equality of treatment The protectionist have no cause to demur because the Clause leaves them alone, so long as the measures taken by them are moderate, in the sense of being determined by the reasonable economic requirements of domestic industries Besides, it helps the protectionists by saving the trouble of complicated and wasteful bargaining which exclusive commercial concessions entail The guarantee of equality of treatment is invaluable[2] No doubt the complicated technique of protection, evolved since the setting in of the depression, has caused serious breaches in the equality of treatment which the Clause has failed to fill up This is largely due to the narrow interpretation put upon the Clause Besides, the Clause cannot be expected to be a panacea for all ills from which the international economic system may suffer It has helped, whenever its help has been sought, to mitigate considerably the rigour even of the present protectionist measures, as shown in the preceding pages Thus the M F N Clause, even under present abnormal conditions, is invaluable for regulating international economic relations and will, undoubtedly, continue to be so in future

But if the Clause is to play its proper part in maintaining the equality of treatment, it is essential that the parties should co-operate in administering the Clause and in observing it not only in letter but also in its spirit

For, as shown above, the letter of the Clause can be legally observed while the spirit may stand trampled Much of the present anarchy in international economic relations is due to the dishonest intentions on the part of several countries to reap the benefits under the Clause and at the same time evade the obligations by narrow interpretation. As adverted to above imperial preference recognised as an exception to the Clause, constitutes the most flagrant breach of the spirit of the Clause, it is a negation of equality of treatment Similarly the development of administrative protectionism has impaired the effectiveness of the Clause Thus, the system of equality of treatment stands to-day seriously challenged by *de facto* discrimination

The most formidable task, therefore, is to remove the menace of discrimination In this task of reconstruction of the economic system, the unconditional M F N Clause can play a valuable part To combat the growing menace, the rigid and narrow interpretation of the Clause should be given up and attempts be made to create low tariff areas by entering into multilateral agreements Similarly, under the present conditions, preferential arrangements between the contiguous countries open for accession to all others, entered into in order to reduce the trade barriers, should be encouraged But, the institution of colonial and imperial preference, which is the worst sore of the modern economic system, should be discouraged and cease to constitute an exception to the Clause A liberal interpretation of the Clause and a more sincere and earnest attempt to work the same in its true spirit is an essential need of the day

The conclusions may be tabulated as follows (1) The M F. N Clause has played an important part in industrial development and continues to render invaluable assistance in the normal functioning of the international economic mechanism The guarantee of equality of treatment is indispensable for the development of world trade

(2) The recent developments in the technique of modern commercial policy, in the form of import quotas, clearing and compensation agreements, etc, have impaired the efficiency of the M F N Clause in securing the equality of treatment in international trade Rigid bilateralism has come in vogue

(3) This is largely due to narrow interpretation of the M F N Clause in order to find an escape from its obligations

(4) A liberal interpretation of the M F N Clause will help a great deal in removing the serious menace of commercial discrimination Further, economic imperialism, in the garb of imperial preference, should be regulated by the M F N Clause To-day, it is one of the important causes of economic and political instability in the world It should cease to be an exception

(5) In view of the present abnormal conditions and complicated trade barriers, the formation of low tariff areas, open for general access should be encouraged by a liberal interpretation of the M F N Clause

CHAPTER VII

TRADE AGREEMENTS PROGRAMME OF THE UNITED STATES

THE growth of the United States tariff policy, as reviewed in the first chapter, records the triumph of vested interests over the economic welfare of the community. Economic prosperity of a community rests upon specialisation on the part of different producing units in the community and the mutual exchange of goods and services turned out by these units. No doubt limited tariff protection of an essentially temporary character can do immense good to a relatively backward country in helping it to consolidate its industrial structure, but the attempt to build up a self-sufficient economic system is both dangerous and wasteful.[1] Self-sufficiency in the modern world is a mirage. Trade barriers can curtail trade, but they cannot entirely eliminate it. The damage to the economic system caused by trade barriers is considerable, the channels of trade are distorted and inefficient industrial enterprises propped up within the protectionist system. In a democratic country these organised vested interests created by the protectionist system exert pressure upon the legislature and try to perpetuate the protection granted to them.

There has been a consistent and cumulative rise in the American tariffs. In the pre-war period, the adverse effects of rising American tariffs were partly neutralised by the debtor position of the United States and the relatively liberal tariff policy pursued by other advanced countries. The Great War brought about basic and far reaching

1 "The unhappy thing about economic nationalism is that the very efforts of a nation to isolate itself intensify the causes of distress and breakdown from which the nation seeks to protect itself. Quota and other limitations to restrict imports prevent other nations from selling exports; currency depreciation to secure a more favourable position in international markets strikes against stability upon which international trade must be built; exchange control to prevent excessive outflows of gold retards if it does not kill, international trade. There can be no selling without buying, no exporting without importing. Consequently, the very measures adopted by nations to protect themselves from the ravages of the disease intensified its virulence and made it the more deadly." Vide F. B. Sayre, Assistant Secretary, address of June 2, 1934.

changes both in the economic position of the United States as well as in the commercial policy of other important countries. The United States emerged from the war a creditor country, destined to receive large payments from the debtor countries by way of interest and principal advanced. The failure on the part of the United States to grasp the full significance of this new situation is largely responsible for the complications of the post-war economic policy. Notwithstanding the shift in her position from a debtor to a creditor status, the United States continued to follow the same obstructive policy of excessive protectionism of the pre-war days, which imperilled her position and led the rest of the world into an economic abyss. In order to safeguard her internal industries against the alleged danger of foreign competition and to ensure the maintenance of a high standard of living, the United States resorted to special tariff protection in the form of an emergency tariff Act of 1921, which was further strengthened by the Fordney Tariff of 1922.

The most obvious result of this excessive increase in American tariff duties was that the difficulties of European debtor countries increased and their economic policies became complicated. Not only was their internal economic recovery retarded, but they found it extremely difficult, due in no small measure to the commercial policy of the creditor countries, to pay their external debts through the export of goods and services. Thus, deprived of the normal methods of discharging their external debt obligations, they were forced to export gold, at the risk of their financial systems. Till the end of January, 1924, the United States had a continuous inflow of gold imports.[1]

This policy of excluding goods and services and accumulating gold had dangerous consequences. Attempts were made to sterilise huge stocks of gold. The Federal Reserve

Banks announced that reserve ratios would no longer be a guide to their credit policy, and that they would conserve this gold, which was bound to be redistributed some day, so that its loss at a later date may not disturb the structure of internal trade and industries Open market operations were resorted to for preventing these fresh stocks of gold being used as a basis for additional credit; the expansion of credit had to be checked The interest rates were kept higher than warranted by the gold reserves This further tended to stimulate the imports of gold Some of this gold flowed into the credit structure and led to the expansion of credit

This is not all The accumulation of huge stocks of gold in the United States caused contraction of credit and fall in prices in those countries which were deprived of their gold reserves by this unprecedented drain There was a marked appreciation in the purchasing power of gold, which added to the difficulties of foreign debtors,[1] the burden of the debt increased Besides, the continuous outflow of gold endangered their currency systems The trade barriers were, therefore, raised by foreign countries in self-defence to protect their currency systems Thus, America's gold accumulating policy was responsible for having given a spur to trade restrictions The Hawley-Smoot Tariff Act of 1930 is a striking example of the hold of vested interests on American legislation, which risked the general economic welfare of the community for placating a selfish minority[2]

Reciprocity Provisions of the American Tariff.—The American practice of bargaining for exclusive favours shows the futility of such a policy from a national as well as an international standpoint Under section 3 of the Tariff Act of 1890, the President was empowered to proclaim, without reference to Congress, specified penalty

1 Their loans had been contracted when the dollar was cheap now they had to meet interest charges on cheap loans when the dollar was more valuable In creating a condition of gold shortage throughout the world America imposed an additional burden of about 10 per cent upon her foreign debtors. The scarcity of dollar exchange due to the reluctance of America to buy outside caused a decline in the foreign gold currencies to the point where additional quantities of gold would be exportable Vide, G E. Putnam Ibid.

2 Vide Jones J M "Tariff Retaliation."

duties on sugar, molasses, coffee, tea, and hides imported from any country, which imposed upon American products such duties and other charges as he deemed to be "reciprocally unequal and unreasonable" Thus, the President had power to place the goods of one nation on a less favourable basis in the American market than the goods of another in case a nation should refuse to grant special favours to American products in its markets Under this law, the President concluded trade agreements with Brazil, Spain, Salvador, the Dominican Republic, German Empire, Great Britain, Austria-Hungary, etc All these agreements were terminated by the Tariff Act of 1894

The tariff Act of 1897 changed the principle of tariff bargaining The first part of section three empowered the President, in return for "reciprocal and equivalent concessions," to grant specified reductions in regular tariff rates Agreements under this provision required neither the ratification of the Senate nor the approval of the Congress Agreements known as the "Argot Agreements," were negotiated with France, Germany, Italy, Switzerland, Spain, Portugal, Bulgaria, the U K, and the Netherlands The United States received reciprocal concessions under each one of these agreements But the most essential point to note about these concessions is that they were in no case exclusive, all that the United States secured was minimum or conventional rates

The second part of section three contains provisions identical to those contained in the Tariff Act of 1890 The President was authorised without reference to Congress, to negotiate commercial treaties in order to secure to the United States special privileges in foreign markets in return for free admission into the American market of coffee, tea, tonka beans and venilla beans Those countries which refused to grant special favours could be penalised by imposing higher duties on their products into the American market

Under Section 4 of the Act the President was authorised to negotiate for concessions in foreign markets and

to concede in return a reduction in the duties of the Tariff Act of not more than 20 per cent of those duties, or to transfer to or to agree to retain on the free list specified articles from any country making satisfactory concessions But the treaties negotiated under it had to be ratified by the Senate and approved by the Congress before they became effective Under this provision treaties known as "Kasson Treaties' were negotiated with Great Britain France Argentine Republic etc The Senate however, refused to ratify these treaties The American experience showed that bargaining for special or exclusive favours was not in the best interests of the country Discriminatory tariff policies make retaliation inevitable and thus sow the seeds of resentment and ill will This policy was therefore given up both in form and principle The Tariff Act of 1909 discarded the principle of bargaining for special favours and instead endeavoured to achieve equality of treatment for the American products in foreign markets

Penalty Provisions of the American Tariff—The Tariff Act of 1909 deleted the reciprocity provision of the Act of 1897 and instituted instead the penalty clauses The duties then imposed were expressly stated to constitute the minimum tariff which could under no circumstances be lowered The maximum schedule could be had by an addition of 25 per cent *ad valorem* to each rate The President was empowered to apply the maximum tariff to the products of those countries which unduly discriminated against the products of the United States Thus, the United States did not offer any reductions in her own minimum tariff and tried to obtain equality of treatment in foreign markets by threats of penalty Such a policy is unsound as subsequent experience has shown beyond doubt

The Act of 1922 introduced similar provisions The President was authorised to impose additional duties on imports from any country which "discriminates in fact" against the United States or 'imposes any unequal imposition or discrimination' If the President finds that

any benefits accrue or are likely to accrue to "any industry *in any foreign country*" *from the imposition or discrimination*, he may cause to be levied additional duties, not exceeding 40 per cent, "to offset such benefits" There was no mention of the minimum tariff in this Act

The Tariff Act of 1930 further strengthened this policy The President was empowered to impose additional duties, up to 50 per cent on imports from any country which imposed on American products any unreasonable charge *which was not equally enforced upon the like articles of* every foreign country Further, if any country maintained or increased its discrimination, the President could completely exclude its products from importation into the United States The minimum tariff was not specifically mentioned

It will be seen that the American tariff policy has consistently tended to exclude imports by raising tariff duties[1] At the same time by negotiating reciprocal trade agreements attempts have been made to increase American *exports* Such *a policy defeats its purpose, for it ignores* the fundamental fact that imports pay for exports No threats can remove this vital contradiction in American tariff policy On the contrary, the threats, by hurting the self-respect of the countries against whom they are held out, introduce dangerous complications in commercial policy

Under such circumstances, the principle of unconditional M F N treatment, which was accepted by the United States in negotiating commercial treaties in 1922, also failed to improve the situation This was, obviously, due to restrictive tariff policy pursued by the United States The underlying spirit of the unconditional *M F N* Clause is that valuable reductions in tariffs, or other trade barriers, shall be made by both the parties negotiating a

commercial treaty, which shall be subsequently generalised to third parties having similar arrangements But the United States never offered any reductions in her tariffs She had her autonomous tariff which was fixed as she liked. The executive (President) had no power to alter it, the legislature dominated by the organised vested interests was in no mood to lower it On the contrary, the duties were consistently pushed up "rigidly and pitilessly" Thus what the United States offered was not an equality of favourable treatment but of equally bad treatment all round In return for this equally bad treatment she insisted that other countries should treat her as well as they treated any third country If any country entered into a commercial treaty with another, containing mutual tariff reductions or other concessions, the United States claimed the same under the uncoditional M F N Clause If the concessions were not immediately and unconditionally extended to her, the President threatened to use his powers by invoking the penalty provisions This pretence of unconditional M. F N treatment is apt to discredit the system. Prof Taussig says "All this constitutes what may be called, to repeat, the club policy We make no offer We fix our own duties quite as we please, and quite unalterably With each successive tariff act, we shove them higher and higher We make them applicable to all countries without mitigation And then we insist that all countries shall in turn treat us as well as they treat any third country If any one of them grants a favour or reduction to another, this must automatically inure to us also If not, the President has the club in his hands He may impose heavy additional duties on their products, he may even exclude them entirely"[1] Such an attitude was bound to defeat its own objective and create international friction and ill-will. In the interests of American trade and industries, apart from any other consideration, this policy had to be reversed.

1 Vide, "Foreign Affairs," 1932-33 p 239

From the foregoing it will be seen that one of the largest barriers to world trade has been the excessively high American tariff The tariff acts of 1922 and 1930 raised the American tariff duties beyond the bounds of legitimate protection Particularly the upward revision of tariff rates in 1930 "definitely contributed to prolonging and deepening the world depression"[1] It gave rise to tariff retaliation, which, coupled with the new methods of trade control, has definitely restricted world trade The world trade declined from 68,622 million dollars in 1929 to 23,288 million dollars in 1934, a decline of about 61 per cent American trade, during the same period, declined from 9,495 to 2,229 million dollars, a decline of 76 5 per cent This economic insecurity led to political insecurity [2] An essential pre-requisite for the restoration of world trade is, therefore, the liquidation of the enormous superstructure of restrictions raised since 1929 In this process of reconstruction and rehabilitation of world trade the United States must play a significant role Prof Taussig rightly suggested that the "whole present policy should be scrapped"[3]

Methods of Reducing Trade Barriers.—There are three devices for the reduction of trade barriers and the liberation of trade policy (1) unilateral tariff revision, (2) multilateral convention, (3) bilateral or mutual lowering of trade barriers Unilateral action will not have the desired effects under the present conditions of world economy The United States could have safely resorted to the unilateral downward tariff revision if the pre-war economic system was still in vogue The abandonment

of the gold standard and the evolution of the new technique of protection during the depression has neutralised the efficacy of unilateral action Under these peculiar economic conditions, the unilateral reduction of tariffs will immediately flood the domestic market with imports This sudden inflow of imports is apt to dislocate domestic industries At the same time, the exports would not record a proportionate increase because unilateral action would not exert sufficient pressure upon foreign countries to give up their extreme protectionist policies[1] The obvious result would be that these unilateral reductions may have to be withdrawn to save domestic industries from the spectre of ruin The downward revision of tariffs to be fruitful must, therefore be reciprocal In short, the unilateral action is ill-suited to the present economic conditions of the world

Can we then expect any substantial assistance from multilateral conventions in the liquidation of trade barriers? Here, too, we find that the present world economic conditions present serious obstructions In these days of economic self-sufficiency and political suspicion it is very difficult to formulate an agreed convention which would serve the interests of all parties alike Besides, a multilateral convention would necessarily require much time to negotiate It would be difficult to evolve any scientific principles as a guide to the downward revision of tariffs The percentage reduction of tariffs, the sole promise under the multilateral system, is far from scientific, it aids the recalcitrant and penalises the sober Again, a multilateral reduction in trade barriers cannot go beyond what the warmest supporters of autarchy are prepared to do Thus,

1 "The method of unilateral reduction of customs duties has possibilities of relative speed and simplicity but is open to a number of serious objections. It offers no assurance that other countries would also reduce their trade barriers at the same time that the United States would embark upon such a course Hence the area of reductions of trade barriers might be seriously restricted. Moreover in the absence of such assurance and, consequently of tangible advantages to be secured by the United States in its export trade it would be extremely difficult to mobilise strong public opinion in favour of substantial reductions in the American Tariff" Vide Leo Pasvolsky "Lloyd's Bank Review" (1935)

at best the ultilateral conventions would touch only the fringe of the problem[1]

Under the present world economic conditions, therefore, the bilateral method, or mutual lowering of trade barriers, is most profitable This method enables a full frontal attack on all forms of trade barriers, tariff as well as non-tariff Besides, it has the advantage of enabling countries to concentrate their attention on those forms of trade barriers which affect them most Again, mutual negotiation is bound to soften the protectionist proclivities of organised vested interests in democratic countries The success in this direction will be more marked if the power of negotiating trade agreements, within definite limits is vested in the executive and the subsequent ratification by the legislature is not required for that would discourage the influence and patronage of the organised minorities in preserving and strengthening the *status quo* The tariff revision effected under expert guidance which executive control usually implies is more scientific and better suited to the interests of the community All the repercussions of the tariff changes are analysed and studied in detail with the assistance of an expert staff, and the mutual discussion between the negotiating countries imparts greater objectivity and softens the rigour of narrow self-interest

Bilateralism is of two types — substantive and formal The substantive bilateralism leads to exclusive trade agreements which breed discrimination and retaliation Exclusive favours granted under this method in which no third country can participate is a constant source of international friction and ill will Such a system helps to raise rather than remove trade barriers Under the formal bilateralism, however the mutual reduction in trade barriers in a given trade agreement are generalised through the M F N Clause to third parties This system should,

therefore, be preferred because it eliminates the possibility of commercial discrimination

In view of the serious dislocation in the structure of American commerce, as a result of tariff retaliation and other methods of trade control there was a complete unanimity among the experts in the United States that an essential prerequisite to the rehabilitation of trade was a radical revision of the commercial policy pursued by the United States As regards the method of revision, the consensus of expert opinion was that it should be effected in such wise as to induce other countries to follow a similar course of action What was most essential was a general revision of the commercial policies of most of the advanced countries, which had resorted to trade restriction The United States, due to her new position[1] acquired during the post-war period, both as a creditor and a highly advanced industrial country, was expected to give a lead in the direction of a more rational commercial policy in her own interests To keep her industrial structure at the highest pitch of efficiency, the United States required markets for her manufactures as well as farm produce and cheap raw materials to feed her industries Besides, as a creditor nation she had to be prepared for a passive trade balance, if her dues were to be promptly paid for The failure on the part of the United States to recognise the full implications of her new economic position was therefore responsible for the erroneous commercial policy and the complications of the post-war period throughout the world, discussed in the preceding pages A more rational and liberal attitude in matters of commercial

policy alone could re-establish international economic equilibrium

Public opinion in America was more inclined towards the bilateral reduction of trade barriers As early as June 1931 Mr Cordell Hull proposed bilateral trade agreements as an effective instrument of a rational and liberal trade policy [1] The supporters of this policy increased as the retaliatory measures taken by foreign countries in consequence of Hawley Smoot Tariff Act of 1930 multiplied American goods found foreign markets gradually bolted against them The reciprocal tariff policy was made an important issue in the first Presidential election of President Roosevelt and the implications of the policy were brought home to the large mass of voters from the press and the public platform The result of the Presidential election showed the faith of the American people in the new American economic policy outlined during the course of the election campaign by the leaders of the democratic party

On March 2, 1934, President Roosevelt requested the Congress to authorise the executive to enter into executive commercial agreements with foreign countries In the course of his message he stated that he wanted this power within carefully guarded limits to modify existing duties and import restrictions in such a way as to benefit American agriculture and industry This shift in the traditional American commercial policy was necessary in view of the startling decline in world trade, and more particularly in the foreign trade of the United States Further, a full and permanent domestic recovery depends in part upon a revived and strengthened international trade and that American exports cannot be permanently

increased without a corresponding increase in imports [1] Thus, the President brought home to the American people the essential interdependence of imports and exports, of domestic and international prosperity This records a remarkable change in American commercial policy

For encouraging American exports, President Roosevelt suggested the method of bilateral trade agreements He said "other governments are to an ever-increasing extent winning their share of international trade by negotiating reciprocal trade agreements If American agricultural and industrial interests are to retain their deserved place in this trade, the American Government must be in a position to bargain for that place with other governments by rapid and decisive negotiations based upon a carefully considered programme, and to grant with discernment corresponding opportunities in the American market for foreign products supplementary to our own" Thus the President asked for an effective bargaining power, which could be promptly exercised, for encouraging America's foreign trade, the power to "make fair offers for fair opportunities"

The Reciprocal Trade Agreements Act of 1934—In view of the foregoing request of the President, the Reciprocal Trade Agreements Act, amending the Hawley-Smoot Act of 1930, was passed and came into force on the 12th June, 1934 The Act empowers the President for a period of three years, to enter into executive trade agreements with foreign countries "for the purpose of expanding foreign markets for the products of the United States, by affording corresponding opportunities for foreign products in the United States" For the purpose of such agreements the President can modify customs duties, impose new trade restrictions, and bind, against change, for the period of a particular agreement, the existing customs treatment accorded to the commodities specified in the agreement.

His power of modifying duties is, however, limited He shall not increase or decrease by more than 50 per cent any existing rate of duty or transfer any articles between the dutiable and free lists This trust reposed in the executive has been sufficiently justified[1]

Implications of the New Trade Policy.—The Trade Agreements Act of 1934 marks a far-reaching change in the commercial policy of the United States[2] Several important principles have been introduced For the first time in the history of American tariff legislation, the Trade Agreements Act recognises the essential principle that an expansion of exports is indispensable to domestic economic prosperity The preamble to the Act emphasises the necessity of increasing American exports "as a means of assisting in the present emergency in restoring the American standard of living in overcoming domestic unemployment and the present economic depression, in increasing the purchasing power of the American public and in establishing and maintaining a better relationship among various branches of American agriculture, industry, mining and commerce" This is a welcome change in American commercial policy

Another important principle underlying the new American commercial policy is the recognition of close interdependence of exports and imports Exports pay for imports To be able to increase her exports America must

be prepared to accept more imports This records a remarkable change in America's traditional tariff policy The President is authorised to exercise the powers granted to him "whenever he finds as a fact that any existing duties or other import restrictions of the United States or any foreign country are unduly burdening and restricting the foreign trade of the United States" and enter into negotiation with foreign governments in order that "foreign markets will be made available to those branches of American production which require and are capable of developing such outlets by affording corresponding market opportunities for foreign products in the United States" In order that the President may be able to demand effectively the equality of treatment for the American products from foreign countries, he is given the discretion to "suspend the application of trade agreements rates to articles the growth, produce, or manufacture of any country because of its discriminatory treatment of American commerce" Thus, the main objectives to be sought are the gradual removal of international trade barriers and equality of treatment for American exports

The unconditional interpretation of the M F N treatment was introduced for the first time in American commercial policy by the tariff Act of 1922 and continued under the Hawley-Smoot Tariff Act of 1930 But, as pointed out above, what America extended in practice was not an equality of favourable treatment, but an equally bad treatment all round Prof Taussig rightly suggested that "this pretence of a general M F N system should be given up" The Tariff Act of 1934, therefore, empowers the President to grant substantial concessions through trade agreements Under the new policy a country entering into a trade agreement with the United States receives the specific reductions in duties contained in the schedules attached to the agreement together with a general promise that any duty reductions granted in future to any other country would also be extended to it automatically and without any compensation Further, in keeping with the spirit of the M F N Clause the duty reductions granted

in an agreement with any particular country are extended automatically and without compensation to all other countries, subject to certain exceptions

The United States has adopted the test of discrimination for generalising the concessions In practice, the policy amounts to a general offer to extend the tariff concessions contained in individual trade agreements to all countries which do not, in fact discriminate against American exports [1] Those countries which follow discriminatory practices cannot claim the concessions granted by the United States in its trade agreements so long as they continue to practice discrimination.[2]

The general rule governing the selection of commodities is that each country receives tariff concessions on those commodities of which it is the principal or major supplier *This basis of granting tariff concessions equips the* United States government with added bargaining strength while negotiating trade agreements with individual countries In other words, by this method the United States can obtain better terms for its exports from other countries than would otherwise be possible

The United States adopts Bilateral Method of Tariff Reduction.—As has been pointed out above, prior to the adoption of the Trade Agreements Act of 1934 the United States was the only industrially advanced country pursuing an "autonomous" tariff policy The result was that the United States could not persuade other countries to reduce the trade restrictions imposed upon her exports This

lack of bargaining power proved a serious obstacle to the expansion of American trade and commerce The bilateral method of tariff reduction was therefore suggested Reviewing the American tariff policy Prof Taussig said

The belief that separate bargains with individual countries now constitute the first step towards a solution of the troublesome problem is based on the international and domestic situation as it now stands An entirely fresh start might indeed conceivably be made by us with a new general tariff act of a reasonable character with general provisions for reductions going far enough to mean something to other countries, and with equality of this favourable treatment for all countries that treated us in like manner Much can be said for a simple and straightforward policy of this kind Much can be said, also against the policy of separate treaties It does often lead to bargaining and bickering It lends itself to pressure by interested persons The negotiators are tempted to try to get the better of each other The result aimed at—a loosening of the restrictions on commerce between nations—is in danger of being buried in the mass of details These dangers and disadvantages inhere in the procedure But it seems now to be the only practicable one for progress towards the goal. Our tariff is too complex and the difficulty of a general overhauling is so great that the problem of revision had best be taken up piece by piece schedule by schedule The same complexities and difficulties appear unhappily in the tariffs of other countries. The world all round is in a situation where the only available course seems to be a patchwork."[1] He further added It is not impossible fortunately that in this case patchwork may lead in the end to something well knit and durable Successive negotiations with the several countries may proceed on similar lines, and may bring harmony in the results The eventual outcome may not be essentially different from what it would be if a most favoured nation programme were laid down at the start Fortunately

the suggestion of Prof Taussig has been accepted and the Trade Agreements Act of 1934 records a change from the "*autonomous*" to the "*conventional*" *tariff system* [1] The progress of the trade agreements programme shows that his expectations are now being gradually realised

It has already been shown that under the present world economic conditions, the formal bilateral method of attacking trade barriers augurs well for liberal trade policy The United States should try to secure a relaxation of those trade barriers which are most injurious to her trade and industries Similarly, the foreign countries entering *into trade agreements with the United States* can concentrate their attention on those commodities which are seriously handicapped in the American market by tariff or other trade restrictions In other words, each trade agreement represents a direct attack upon those trade barriers in the two countries which are particularly obstructive to their mutual trade Thus, the bilateral method is more effective than the unilateral downward revision of the tariff Besides, under the bilateral method more substantial reduction of trade barriers can be effected due to mutual reciprocity From the standpoint of the United States, therefore, after a sufficient number of trade agreements have been concluded and the tariff reductions embodied in each have been generalised through the operation of the unconditional M F N principle, the final result will be much better than that which could be had *under unilateral reduction*

Another important feature of the Trade Agreements Act *is the absence of any requirement of legislative sanction* of the trade agreements concluded under the Act This is a very significant change in the traditional American tariff policy The history of American tariff shows that the trade agreements programme would not have succeeded in practice were the agreements contingent upon legislative ratification Prof Taussig had suggested earlier that

"the executive should have authority to offer favours definitely—something in the way of an assured reduction of duty It is hopeless to expect any consistent or effective action if each individual treaty must have a two thirds vote in the Senate "[1] Thus, the Trade Agreements Act augurs well for the future The President it is hoped, will use his power in combating the traditional excessive protectionism at home and autarky abroad, he can give a lead in the reconstruction of world economic policy and the restoration of the distorted channels of trade to their normal form

The Commercial Treaties under the Trade Agreements Act—It is now necessary to review the progress of the reciprocal trade agreements programme and the difficulties encountered in the process of negotiation The number of trade agreements entered into with foreign countries, the dates on which they were signed and came into effect may be seen from the following table —

Country	Signed	Entered into force
Cuba	24– 8–1934	3– 8–1934
Brazil	2– 2 1935	1– 1–1936
Belgium	27– 2–1935	1– 5–1935
Haiti	28– 3–1935	3– 6–1935
Sweden	25– 5–1935	5– 8–1935
Columbia	13– 7–1935	20– 5–1936
Canada (2)	15–11–1935	1– 1 1936
Honduras	18–12 1935	2– 3–1936
Netherlands and Colonies	20–12–1935	1– 2–1936
Switzerland	9– 1–1936	15– 2–1936
Nicaragua	11– 3 1936	1–10–1936
Guatemala	24– 4–1936	15– 6–1936
France and Colonies	6– 5–1936	15– 6–1936
Finland	18– 5–1936	2–11–1936
Costa Rica	28–11–1936	2– 8–1937
El Salvador	19– 2–1937	13– 5–1937
Czechoslavakia	7 3–1938	16– 4–1938
Ecuador	6– 8–1938	23–10–1938
United Kingdom	17–11–1938	1– 1–1939
Turkey	1– 4–1939	5– 5–1939
Venezuela	6–11–1939	16–12–1939
Iraq	3–12–1938	19– 6–1940

In addition to the foregoing agreements, there have been a few other commercial understandings which should be noted for a proper appreciation of the reciprocity programme The first is a provisional commercial agreement with Czechoslovakia in the form of an Exchange of Notes, signed at Washington on March 29, 1935, under which the parties agreed to grant each other unconditional most-favoured-nation treatment with regard to export and import duties and all regulations affecting the sale, taxation or use of imported goods Fair and equitable treatment was stipulated with regard to exchange control, quotas and to the imposition of a lower duty on the importation or sale of a specified quantity of an article than that imposed on importation in excess of the specified quantity Advantages accorded by either party to facilitate frontier traffic or resulting from a customs union were excluded from the operation of the agreement Advantages accorded by the United States to the Phillippine Islands the Panama Canal Zone and Cuba were likewise excluded, as were advantages accorded by Czechoslovakia to Austria, Hungary, Yugoslavia and Roumania [1] This understanding was subsequently replaced by the trade agreement signed on March 7, 1938 [2]

The second is the Exchange of Notes on trade relations between the United States and the USSR on July 24, 1935 [3] The Exchange of Notes provides that the U S S R is to enjoy the benefit of the reduction of duty made by the U S A Government as a result of the trade agreements concluded in pursuance of the 'Act to amend the Tariff Act of 1930" Exception is made for reductions in the United States Tariff in respect of goods imported from Cuba The Soviet Government, in return, undertook to increase substantially its purchase of United States' goods This agreement was to remain in force for one year but was extended for another year In 1937, a new agreement was entered into providing for unrestricted and uncondi-

tional most favoured nation treatment for a period of one year[1] The tenure of this agreement has been extended

A commercial modus vivendi with Chile was signed on January 6 1938 This modus vivendi, which replaces the Exchange of Notes between the two Governments dated September 28 1931 continues to extend most favoured-nation treatment mutually as provided in the earlier agreement The Government of Chile also undertakes to abolish the exchange control measures affecting the United States' goods as soon as the international economic situation allows Until then the Government of Chile will avoid exchange control measures involving the use of exchange at rates higher than those set by the free supply and demand of the market[2]

The intention to negotiate trade agreement with Spain was announced on September 17 1934 and with Italy on January 16, 1935 but the negotiations were later on suspended. The rigid bilateral commercial policy pursued by Spain and the Civil War created difficulties in the progress of negotiations Similarly, the Italian policy of substantive bilateralism and the Italo-Ethiopian conflict were responsible for the suspension of negotiations with Italy

As regards the actual progress we find that during 1934 only one trade agreement was signed and came into effect In 1935 eight agreements were signed, of which three became effective Six agreements were signed in 1936 and ten agreements became effective The trade agreement with Salvador was the only one signed during 1937 During 1938 was signed the modus vivendi with Chile and trade agreements with Czechoslovakia, the United Kingdom and Canada. The Anglo-American trade pact is of great significance in modern commercial policy It has given a shock to the British Imperial Economic System built up at Ottawa and marks the inception of an era of relatively freer

international trade In 1939, two trade agreements were signed and both became effective

The progress of the reciprocal trade agreements programme, outlined above, has been rather halting and half-hearted Misgivings have been caused in certain quarters The President has been invested with fairly wide authority and it is not unnatural to expect a prompt and vigorous drive for lowering trade barriers, through reciprocal trade agreements, and expansion of American trade [1] That the progress has been slow is accepted at all hands But to throw the blame entirely upon the executive is to ignore the essential facts of the situation Several circumstances conspired to retard the progress of the programme The most important factor to be noted in this connection is the necessity of a critical and exhaustive analysis of the economic implications as a condition precedent to the starting of negotiation for a trade agreement with a foreign country The executive has had to move cautiously and carefully The United States Government has organised an elaborate machinery for the negotiation of trade agreements [2] The collection and collation of exhaustive data under expert guidance coupled with expert technical advice ought to constitute the basis of any change in modern commercial policy All this takes time Similarly, the foreign countries also collect the necessary data for preparing their cases Thus, there was to some extent unavoidable delay To this must be added the difficulties created by the protectionist vested interests Mr Sayer, the Assistant Secretary of State stated 'The supreme obstacles are the political ones Every time it is proposed to lower a tariff the lobbyists and politicians descend upon Washington and intense pressures are brought to bear upon those responsible for decisions "[3] Another important

obstacle has been the policy of rigid substantive bilateralism pursued by a number of countries[1] The United States has always pressed for the removal of discrimination and arbitary diversion of trade as a preliminary to the negotiations of a trade agreement This adjustment in commercial policy cannot be easily effected, delay is inevitable The New Deal legislation and the Hull-Peck controversy are also responsible for the slow progress of this new liberal trade policy

The Structure of Reciprocal Trade Agreements

(1) The unconditional Most-Favoured-Nation Clause — We shall now analyse the texts of the trade agreements in detail in order to find out the more important features in their structure, which will enable us to understand better the implications of the new commercial policy In the preceding section we have noted, in brief, the implications of the new policy and the changes it has effected in the traditional attitude of the United States in matters of trade and the barriers obstructing the normal flow of trade In this connection the most welcome feature of the new programme is the adoption of the unconditional Most-Favoured-Nation Clause, coupled with the reciprocal reduction of duties[2] This marks the end of the "club policy" and the dawn of an era of "an equality of favourable treatment," as it is coupled with substantial tariff concessions unknown before Almost every agreement guarantees unconditional most-favoured-nation treatment For instance, the trade agreement with Brazil,[3] provides as follows

"Any advantage, favour privilege or immunity which has been or may hereafter be granted by the United States of America or the United States of Brazil in regard to the above-

mentioned matters, to a natural or manufactured product originating in any third country or consigned to the territory of any third country shall be accorded immediately and without compensation to the like product originating in or consigned to the territory of the United States of Brazil or the United States of America respectively"

Thus, the M F N Clause provides for the automatic extension of tariff concessions, given in the past and those that may be granted in future, immediately and without compensation

Similarly, the trade agreement with Canada[1] *provides for* unconditional and unrestricted most-favoured-nation treatment as follows —

"Any advantage favour privilege or immunity which has been or may hereafter be granted by Canada or the United States of America in regard to the abovementioned matters, to a natural or manufactured product originating in any third country or consigned to the territory of any third country shall be accorded immediately and without compensation to the like product originating in or consigned to the territory of the United States of America or Canada respectively, and irrespective of the nationality of the carrier"

The scope of the M F N Clause is unrestricted For instance, the trade agreement with Canada provides as follows —

"Canada and the United States of America will grant each other unconditional and unrestricted most-favoured-nation treatment in all matters concerning customs duties and further, in all matters concerning the rules formalities and charges imposed in connection with the clearing of goods through the customs and with respect to all laws or regulations affecting the sale or use of imported goods within the country"

As regards the internal taxes and levies, there is usually an article specifying national treatment in addition to the most-favoured-nation treatment For instance, the trade agreement with Canada[2] provides

"*Articles the growth produce or manufacture of Canada or* the United States of America, shall, after importation into the

other country, be exempt from all internal taxes, fees, charges or customs duties other or higher than those payable on like articles of national origin or any other foreign origin."

"The provisions of this Article in regard to granting of national treatment shall not affect the laws now in force in Canada whereby leaf tobacco, spirits, beer, malt and malt syrup imported from abroad are subject to special taxes nor shall they affect the applicability to goods produced or manufactured in the United States of America or special excise taxes imposed under existing provisions of the special War Revenue Act In these respects however most-favoured-nation treatment shall apply"

The most-favoured nation provisions have been used by the United States to regulate the quotas imposed by the foreign countries on American goods The quotas are to be so used as not to cause discrimination The quota restrictions would not amount to discrimination if the share allotted to the United States is equivalent to the proportion of the trade which it actually enjoyed during a previous "representative period" The "representative period" has been officially defined as a series of years during which trade in a particular article was free from restrictive measures of a discriminatory character and was not affected by unusual circumstances such as, for example, a crop failure in the case of an agricultural product For instance, the trade agreement with Canada provides that "in the event of quantitative restrictions being established by either Canada or the United States of America for the importation of any article it is agreed that in the allocation of the quantity of the restricted goods which may be authorised for importation, the other country will be granted a share equivalent to the proportion of the trade which it enjoyed in a previous representative period prior to the establishment of such quantitative restrictions" This representative period is to be determined by mutual consultation by the parties to the agreement. The quotas, thus fixed, are taken to accord fair and equitable treatment. Thus, the quotas have been placed within the scope of the Most-Favoured-Nation Clause.

The same rule is applied to the allocation of foreign exchange under any system of foreign exchange control Most of the trade agreements provide that if any of the parties to the agreement establish or maintain a control of the foreign exchanges they will accord to the nationals and commerce of each other the most general and com plete application of the unconditional most favoured nation principle For instance the trade agreement with Canada provides as follows

> Thus tariff advantages and other benefits provided for in this agreement are granted by Canada and the United States of America to each other subject to the condition that if the government of either country shall establish or maintain any form of control of foreign exchange it shall administer such control so as to ensure that the nationals and commerce of the other country will be granted a fair and equitable share in the allotment of exchange With respect to the exchange made available for commercial transactions it is agreed that the Government of each country shall be guided in the adminis tration of any form of control of foreign exchange by the principle that as nearly as may be determined the share of the total available exchange which is allotted to the other country shall not be less than the share employed in a previous repre sentative period prior to the establishment of any exchange control for the settlement of commercial obligations to the nationals of such other country The grant of reciprocal trade concessions is subject to the condition that the parties shall be accorded fair and equitable treatment in administration of exchange control already established or that may be established in the future

Thus the exchange control is also brought within the scope of the Most Favoured Nation Clause

The most favoured nation principle has also be to control the working of monopolies The Ar suppliers are to be accorded fair and equitable treat This is secured by the provision in the trade agreem that the purchases of these monopolies will be influenc solely by those considerations such as price qualit marketability and terms of sale which would ordinarily be taken into account by a private commercial enterprise interested solely in purchasing such products on the most

Thus, it will be seen that these new methods of trade control have been brought within the purview of the Most-Favoured-Nation Clause and suitably regulated so as to provide equality of favourable treatment feasible under the present conditions

(ii) **Quota Provisions in the Trade Agreements**—Another important feature of the new American trade agreements programme, as will be seen from the foregoing discussion, is the inclusion of quota provisions in the trade agreements in order, it is claimed, to enable the Government of the United States to reduce their restrictive effect upon American trade, and, at the same time, show the futility of such a policy How far the United States has succeeded in combating the dangerous consequences of the quota system by the trade agreements' programme we now propose to analyse

The general provisions regulating quota arrangements, to be found in most of the trade agreements, may be briefly reviewed Here we find the common provision that quantitative restrictions are not to be imposed on the articles enumerated in the schedules attached to the agreements, except under specified conditions For instance the trade agreement with Canada provides —

"No prohibition, import or customs quotas, import licenses, or any other form of quantitative regulation shall be imposed by Canada on the importation or sale of any article produced in the United States of America and enumerated in Schedule I nor by the United States of America on the import or sale of Canadian articles enumerated in Schedule II, except as specifically provided for in the said schedule"

This clause provides sufficient safeguard to the contracting parties against the value of their concessions being impaired by subsequent manipulations of the quota system Besides it prevents more frequent changes in quota regulations and imparts stability to trade relations The mutual assurances given by the parties not to control trade by quantitative regulations shows that they recognise the futility of these measures and are prepared to discard them if assured that the other countries trading with them are likewise willing to do so In other words, people usually want protection against the dangerous consequences of such measures and use them in self-defence

To this however, there are important recognised exceptions For instance, the trade agreement with Canada provides that quantitative restrictions may be "imposed by either party on the importation or sale of the article of any other country in conjunction with governmental measures operating to regulate or control the production market supply, or prices of like domestic articles, or tending to increase the labour costs of production of such articles" Similar provision is made in most of the other trade agreements But at the same time, stipulation is made in these agreements that whenever the Government of either country propose to establish or change any restriction authorised by this paragraph, it shall give notice thereof in writing to the other Government and afford it an opportunity for consultation within 30 days of the receipt of the notice, and if an agreement is not reached within these thirty days the Government which proposes to take the action shall be free to do so, but the Government adversely affected thereby may within fifteen days after the imposition give written notice and at the expiration

on certain industrial products to approved American organisations The unused portions of industrial quotas of the previous quarter will be taken into account while allocating the quota for the subsequent quarter When the American quotas according to French statistics are found to be exhausted, the United States Government will be informed and given an opportunity to present its case, if any, before further imports are barred The imports in excess of the quota allotted for any period will be charged against the quota of the following period

The "representative period" formula shall be the basis for the allocation of quotas on the articles which though subject to quantitative restrictions are not included in Schedule III But there is an additional stipulation regulating the allocation of quotas to this group of articles The stipulation provides that in the case of articles where imports in the past year prior to the imposition of quantitative restrictions were 10 per cent or more, the quotas allocated to the United States of America shall not be less than 10 per cent In those cases where imports were less than 10 per cent, the quotas shall be fixed at the amount imported in that year This stipulation however, like the one discussed above, savours of discrimination, and constitutes an important inconsistency in the United States' most-favoured-nation policy This method needs prompt modification

The United States has acquired from France substantial quota concessions on most of the commodities But it has not been able to achieve full consolidation of these concessions due to the French practice of retaining freedom of action in matters of commercial policy, particularly the regulation of quotas Under certain specified conditions France has retained the liberty of changing quota concessions Notwithstanding these provisos, France has surrendered her liberty of action to a very important degree. In short, the agreement has protected adequately American commercial interests and is an important milestone towards freer international trade

The Cuban trade agreement provides for a reduction in duty from 1 5 to 90 cent per pound on Cuban sugar imported into the United States Even this lower duty was equal to approximately 100 per cent of the Cuban price But when sugar was brought within the scope of the Agricultural Adjustment Act in 1934, quota restrictions were imposed on the Cuban sugar imported into the United States and the reduced duties were thereafter applicable only to the quota assigned to Cuba Consumers in America suffered These quota arrangements have definitely restricted imports into the United States Mr Bidwell says "the restrictions on imports of Cuban and Philippine sugar are real restrictions they have succeeded in accomplishing the standard results of quantitative restrictions, i e, they have not only raised domestic sugar prices, but also have insulated our prices from the fluctuations of world market prices" American consumers of sugar have paid a heavy cost For instance, in 1936, according to the Department of Agriculture estimates, American consumers paid \$350 million more for the commodity than it would have cost them at world market prices

Quantitative restrictions have been imposed on the Cuban tobacco imported into the United States The quantity imported for consumption may not exceed 18 per cent of the total quantity of tobacco used in the manufacture of cigars during the preceding calender year Under the trade agreement duty on tobacco is reduced from \$3 60 per pound and 20 per cent *ad valorem* to \$2 25 per pound and 12½ per cent *ad valorem* An additional stipulation provides that higher duty will again become effective in the event of the domestic control of tobacco under the Agricultural Adjustment Act is abandoned Later both the duty concession and the quantitative restrictions on tobacco have been withdrawn

The Canadian agreement also contains quantitative restrictions on the imports into the United States which

1 Vide Dr Tasca p 223

compete with domestic production. As a result of these restrictions the value of concessions is considerably neutralised For instance tariff quota is imposed on imports of cream The duty is reduced from 56 6 cents to 35 cents per gallon, but, the reduced duty is applicable only to 1,500 000 gallons of imports whereas the average imports of cream during 1923-32 amounted to 4 392 000 gallons In short, the value of present concessions is limited. There is, however, very wide scope for liberalising the concessions The ' tremendous American market " is invaluable to the Canadian producers

The most recent case of the establishment of customs quota by the United States in connection with tariff reductions made through the Trade Agreements Programme is the customs quota on fuel oil and crude petroleum established in the Venezuelan agreement The import tax on these products has been halved for an amount not exceeding 5 per cent of the total crude petroleum processed in the United States refineries during the previous year Imports in excess of this quota will have to pay the original tax A subsequent proclamation issued by the President has assigned shares in the quota to the principal suppliers of the United States Mexico, which used to supply about 10 to 15 per cent of the total oil imports to the United States, before the expropriation, was assigned a very small share Venezuela was assigned 71 9 per cent of the quota, the Netherlands and its empire 20 3 per cent., Columbia 4 per cent., and all other countries including Mexico 3 8 per cent The injustice is caused to Mexico by selecting a "representative period" as a base which was not representative The oil imports for the first ten months of 1939 could not be said to be "representative period." for Mexican share which was about 13 per cent from 1929 to 1938 had fallen in the latter year to 5 4 per cent and fell further in 1939, owing to the boycott of Mexican oil by the expropriated companies Thus, these quota arrangements violate the principle of "equality of treatment" and impair the effectiveness, both economic and moral, of the Trade Agreements Programme

(iii) Exchange Provisions in the Trade Agreements.— That exchange restrictions are placed within the purview of the Most-Favoured-Nation Clause and the method of allocation regulated thereby has already been noted The resulting equality of treatment in the administration of these new trade deflecting devices — clearing, payments, compensation, and barter arrangements — is a remarkable and valuable step in the direction of freer world trade The provisions of the Canadian trade agreement, quoted above, show that the parties agree to administer the control of foreign exchange in such a way as to ensure that the nationals and commerce of the other country will be granted a fair and equitable share in the allotment of exchange The benefits accorded under the agreement can be availed of only so long as this principle is strictly adhered to Further, the parties agree to give sympathetic consideration to complaints affecting variation in the rates of exchange and the administration of these measures, and in case no suitable understanding is arrived at, the aggrieved party may terminate the agreement For example, the Canadian agreement provide as follows —

'In the event that a wide variation occurs in the rate of exchange between the currencies of Canada and the United States of America the Government of either country, if it considers the variation so substantial as to prejudice the industries or commerce of the country shall be free to propose negotiations for the modification of this agreement and if an agreement with respect thereto is not reached within thirty days following receipt of such proposal the Government making such proposal shall be free to terminate this agreement in its entirety on thirty days written notice

This provision, known as the Belgian Clause," is found in most of the agreements and provides sufficient protection against wanton currency manipulations neutralising the concessions accorded in the trade agreements But the wording of the clause is significant The parties are expected to resort to this clause only in the event of a "wide variation" which is "so substantial as to prejudice the industries or commerce of the country", it has to be sparingly used Further, the clause gives full opportunity

for mutual discussion and understanding of each other's view point This is invaluable in as much as a full, frank and cordial discussion would clear many misapprehensions and effect amicable adjustment The wide powers of terminating the agreement in its entirety vested in the parties are apt to promote better understanding

The Cuban trade agreement is very interesting because it consolidates the exchange restrictions The parties to the agreement undertake to refrain from subjecting payments to any regulation restriction, charge or exaction other or higher than was in force on April 1 1934 This clause prevents fresh resort to exchange control All other trade agreements entered into by the United States permit full latitude for the use of exchange control and claim only equality of treatment in their administration as secured by the Most Favoured Nation Clause

The Brazilian trade agreement is significant because this is the only country from which the United States have succeeded in securing a definite undertaking for the liquidation of frozen debts According to the agreement the Bank of Brazil agrees to allot exchange for the settlement of all current commercial claims and sufficient exchange to liquidate gradually blocked balances due to American importers The amount of exchange allocated to the United States is to be slightly more than the share of American exports to Brazil formed in the latter's total imports during a "representative period (previous ten years) This clause savours of discrimination it violates the principle of equality of treatment in the allocation of foreign exchanges.

(iv) **Tariff Concessions in the Trade Agreements**—The growth of economic nationalism during the post war period has led to excessive rise in tariff barriers The avowed purpose of the reciprocal trade agreements programme of the United States is to demobilise these tariff barriers. As Mr F B Sayer the Assistant Secretary of State said "the American programme of trade agreements

is an effort to combat and defeat these destructive tendencies" To achieve this objective the United States must adopt a liberal attitude in working the new trade agreements programme *Prohibitive tariff barriers must be* lowered if international trade is to be revived and economic equilibrium established In this section, therefore, the trade agreements will be analysed in order to find out the nature of tariff concessions accorded therein

The tariff concessions are in the main, of three types duty reductions, duty bindings, and "freezing" of free list items In the first case, specific duty reductions are granted on definite articles noted in the schedules attached to the agreements The second form of concessions consists of the undertaking given by the parties not to raise these rates The rates may, however, be lowered In the third case, the parties to the agreement undertake not to impose duties on articles on the free list, incorporated in the agreement

Duty Reductions.—As regards duty reductions, most of the trade agreements have schedules containing reduced duties on the articles specified therein of importance to the export trade of the parties concerned together with an undertaking that during the currency of the agreement the rates shall not be raised The clause runs as follows

> "Articles the growth produce or manufacture of enumerated and described in schedule annexed to this *agreement and made a part thereof shall upon their importation* into be exempt from ordinary customs duties in excess of those set forth and provided for in the said schedule"

The actual quantum of duty reductions accorded in the various trade agreements by the parties concerned differ according to the tariff policy pursued by them In some cases tariff reductions play a relatively minor role because the tariff barriers raised by these countries have been moderate as compared with those of other countries This is so in the case of trade agreements with France, Sweden,

the Netherlands and Finland For instance the reductions in the French minimum tariff were as follows [1]

Article		Minimum Tariff Duty old (Per 100 kilgos)	New
Grapefruit		100	50
Sewing machine heads		800	700
Cash registers and similar machines		1 200	900
Chasses for passenger motor cars	(a) per kilgo	8 30	4 15
	(b)	9 60	4 80
	(c)	10 90	5 45
	(d)	13 25	6 65
	(e)	16 10	8 05
Penholders		20	13
Metal fittings for all articles		30	25
Fountain Pens		2 each	1 50
Sparkling plugs		8 20	2 85

This table gives us a definite idea of the nature of tariff concessions accorded by France The duty reductions are fairly substantial Much more valuable concessions have been obtained from France in quota restrictions which she has used more extensively as an instrument of trade control

In return for the tariff and non tariff concessions accorded by France the United States granted tariff concessions on wines cigarette paper machine-made lace perfumes and essential oils broad silks and rayon woven fabrics gloves corset and elastic fabrics tinsel products etc The modifications in the tariffs of the United States were as follows —

Articles		Old	New
Cellulose		80% *ad val*	40% *ad val*
Oils		25% *ad val*	12½% *ad val*
Carbons and electrodes	(a)	60% *ad val*	40% *as val*
	(b)	45% *ad val*	30% *ad val*
Bottles and Jars		75% *ad val*	37½% *ad val*
Prism binoculars		60% *ad val*	45% *ad val*
Beltings		45% *ad val*	30% *ad val*
Brandy		$5 per proof gal	$2.5 per proof gal
Champagne		$6 per gal	$3 per gal
Pile ribbons		62½% *ad val*	50% *ad val*

1 Vide B. T J 11-4-1936, P 876

Thus the maximum reduction in duties was of 50 per cent

Sweden received tariff concessions on newsprint, woodpulp paper board wrapping paper, wire rods, special irons and steels matches unmanufactured granite, pocket knives, certain tools, enamelled household utensils, etc The following table[1] gives a definite idea of the nature of duty reductions accorded by the United States on Swedish articles —

Articles	Rates of Duty Old	New
Compounds of cellulose	*30% ad val*	*20% ad val*
Lighthouse lenses (a)	*40% ad val*	*25% ad val*
" " (b)	*35% ad val*	*25% ad val*
Granite paving blocks	*60% ad val*	*40% ad val*
Ferrochrome	*30% ad val*	*25% ad val*
Round iron or steel wire	*25% ad val*	*20% ad val*
Mill saws	*20% ad val*	*12% ad val*
Utensils	*30% ad val*	*15% ad val*
Calculating machines	*35% ad val*	*25% ad val*
Scythes sickles etc	*30% ad val*	*20% ad val*

The United States, in return received duty reductions on a number of articles, 61 6 per cent of the total American exports to Sweden benefitted from the reductions[2]

In the case of the trade agreement with the Netherlands the United States did not receive duty reductions, the main concessions consisted of the relaxation of import quotas and other new measures of trade control The tariff barriers are not very formidable in this case In return for substantial concessions in non-tariff trade barriers the United States offered tariff concessions ranging up to 50 per cent The following table[3] gives an idea of the modification in the American customs tariff resulting from the trade agreement with the Netherlands

1 Ibid 25 7 1935 pp 154-55
2 Vide Dr Tasca p 172
3 Vide B T J 6 2 1936 pp 215 16

Articles	Rates of Duty Old	New
Amyl Alcohol	6c per lb	4c per lb
Laundry soap	25% *ad val*	15% *ad val*
Amyl Acetate	7c per lb	4c per lb
Glycerin	2c per lb	⅓c per lb
Potato Starch	2½c per lb	½c per lb
Dexterine	3c per lb	2¼c per lb
Electrical X ray apparatus	35% *ad val*	17½% *ad val*
Bulbs	30% *ad val*	15% *ad val*
Cocoa butter	25% *ad val*	12½% *ad val*
Cords and twines	40% *ad val*	20% *ad val*
Pile fabrics	50% *ad val*	30% *ad val*
Hats	25% *ad val*	12½% *ad val*

The trade agreement with Switzerland like that with France is interesting in that it combines reduced duties with more liberal quotas Switzerland reduced its customs duties on fruits jams and certain types of machines and increased the United States quota of wheat jam lard and automobiles In return for these concessions the United States reduced its duties on fine cotton clothes including fine organdies knit underwear special silks watches and parts certain chemicals and coal tar dyes Swiss cheeses machine embroidered articles special types of machinery etc The United States customs tariff was modified as follows[1]

Articles	Rates of Duty Old	New
Chloroacetic acid	5c per lb	2½c per lb
Perfume materials (a)	45% *ad val*	30% *ad val*
Perfume materials (b)	45% *ad val*	22½% *ad val*
Steam boilers	35% *ad val*	20% *ad val*
Laboratory instruments	40% *ad val*	20% *ad val*
Jig boring tools	30% *ad val*	15% *ad val*
Knitting machines	40% *ad val*	27½% *ad val*
Hydraulic reaction turbines	27½% *ad val*	15% *ad val*
Rivets nuts and washers	45% *ad val*	30% *ad val*
Screws	45% *ad val*	30% *ad val*
Knit underwear	*45% ad val*	*30% ad val*

There is another group of trade agreements in which duty reductions have played a very important part For

1 Vide B T J., 13-7 1936 pp. 248-51

instance, the Canadian trade agreement, which became effective from January 1, 1936, embodies substantial duty reductions on both sides Canada reduced duties on 767 tariff items, the total imports of which from the United States of America amounted to over $400 million in 1903 [1] The Canadian tariff rates were lowered in two ways Firstly, the Canadian intermediate tariff schedules were extended to all American products, in accordance with the most-favoured-nation principle Secondly, designated reductions in rates were made upon a selected list of products important in the American export trade with Canada These tariff reductions are "almost without contemporary parallel"[2]

The effective utility of these tariff concessions is further increased when it is recalled that the Canadian Government agreed to modify its use of arbitary valuations in the application of *ad valorem* duties to American products This arbitary valuation had raised the level of duties and created uncertainty as to their future, obstructing thereby the flow of American exports to Canada The removal of this serious handicap on American exports was, therefore, invaluable Emphasising the significance of this change in the practice of valuation the Canadian Prime Minister said [3] "Not less important than the visible and conspicuous reductions in the rates of duty applicable to imported goods has been the elimination of the arbitrary and often invisible interference of governmental agencies in the normal course of trade We have cancelled scores of arbitrary valuations, limited the scope of the application of the dumping duty to the protection of the legitimate and substantial domestic interests '

In return, the United States granted valuable concessions on certain Canadian agricultural products, whisky, patent leather, harness leather and acetic acid The concessions on timber, cattle cream and seed potatoes were, however, granted on limited quantities only

The trade agreement with Brazil is also important from the standpoint of tariff reductions Of the 67 items covered by the duty reductions, on 49 items the reductions varied between 20 and 39 per cent In return the United States also offered valuable tariff concessions The nature of tariff concessions offered by the U S A can be gauged from the following table [1]

Articles	Rates of Duty Old	New
Copaiba balsam	10% *ad val*	5% *ad val*
Specac	10% *ad val*	5% *ad val*
Mate	10% *ad val*	5% *ad val*
Manganese ore	1c per lb	½c per lb
Castor beans	½c per lb	¼c per lb

The trade agreement with Salvador is very significant in the sense that of the sixteen items covered by the agreement, the tariff reductions offered by Salvador were 60 per cent and over on thirteen items The reductions in Salvadorean customs duties were as follows [2]

Articles	Rates of Duty Old	New
	(U S dols per	100 kilgos)
Ham, except tinned ham	51 40	12 00
Salmon tinned	29 29	5 00
Oatmeal	8 80	4 40
Fresh fruit	5 00	2 50
Dried fruit	24 81	5 00
Tinned vegetables	29 29	6 00
Tinned fruit	29 29	7 50
Rubber tyres not specified	30 00	10 40
,, ,, for automobiles and aircraft	30 00	10 40
,, ,, for motor cycles and bicycles	30 00	10 40
Inner tubes	30 00	10 40
Phonographic records	75 00	18 60

The Czechoslovakian trade agreement also brought substantial tariff reductions to the United States The reductions in the Czechoslovakian customs duties were as follows —[3]

1 Vide B T J 13-1 1936 p. 153.
2. Ibid, 3-6-1937
3 Vide B. T J., 17-3-1938 p 397

Articles	Import Duty Old	New
	(Per 100 kilgos)	
Raisins	240	180
Grape fruit	30	25
Walnuts	90	80
All dried fruit	120	60
Other preserved vegetables	600	200
All other preserved fruit	560	360
Fruit and berry juice	1,200	200
Chewing gum	1,200	720
Mineral oils semi refined	*85*	*65*
Rock wool	40	free
Motor cycles	1,700	1 400
Refrigerator cabinets	3 000	1 000
Complete passenger automobiles	2 700	1,700
Complete trucks	1,900	1,700
Motor vehicle parts	2 700	1 700

From the foregoing brief review it will be seen that substantial tariff reductions have been effected as a result of the trade agreements' programme The effective value of these duty reductions is much higher since they are generalised through the Most-Favoured-Nation Clause But the United States should adopt a more liberal attitude and accelerate thereby the pace of demobilisation of these tariff restrictions

Duty Bindings—In order to understand the full implications of the tariff concessions, it is necessary to note that most of the trade agreements contain a pledge binding the tariff treatment accorded to certain goods against increase For instance the Canadian trade agreement contains an undertaking to the effect that "articles the growth, produce or manufacture of the United States of America enumerated and described in Schedule I and annexed to this agreement shall, on their importation into Canada, be exempt from ordinary customs duties, taxes, fees, charges or exactions, imposed on or in connection with importation in excess of those imposed on the day of the signature of this agreement or required to be imposed thereafter under laws of Canada in force on the day of the signature of this Agreement" This pledge

imparts tariff stability which is indispensable for the development of modern trade and industries Besides, it puts a definite check on the hectic race for raising tariffs At the same time it is significant to note that the door for further reductions in duties is kept wide open

"Freezing" the Customs Free List—Some of the trade agreements contain an undertaking that the goods on the free list shall not be transferred to the dutiable list The trade agreements with Canada, Sweden, Netherlands, and Finland accord such an assurance

(v) Provisions Regulating Administrative Protectionism.—It has been shown that administrative protectionism plays an important part in the modern technique of protection,[1] its use has become more frequent since the setting in of the trade depression The discrimination inherent in administrative protectionism has been a constant source of friction between nations, not infrequently it has led to violent and destructive tariff wars The recent developments in this technique and its extensive use constitute a most formidable obstacle to the development of international trade Any frontal attack on trade barriers, therefore to be effective, must bring within its ambit these new protectionist devices and regulate them so as to minimise their restrictive effects

Most of the trade agreements entered into by the united States under the reciprocal trade agreements programme contain specific provisions regulating the scope and methods of administrative protectionism For instance, the trade agreement with Sweden[2] provides that "articles the growth, produce, or manufacture, of the United States of America enumerated and described in the schedule are to be exempt on importation into Sweden from customs duties higher than those set forth in the schedule and from all other duties, taxes, fees, charges, or exactions imposed on or in connection with importation, higher than those

required to be imposed on the day of the signature of the Agreement or required to be imposed thereafter under laws of Sweden in force on the day of the signature of the Agreement' The United States accords a similar pledge to the Swedish goods It is needless to add that the binding contained in the foregoing clause is valuable, since it limits the scope of discrimination

Further, most of the trade agreements contain a stipulation that no preferential treatment is to be accorded to domestic producers or those of any third foreign country with respect to internal taxes or charges except as provided by the laws of either country in force on the day of the signature of the agreement This clause provides for national as well as most-favoured-nation treatment, both "inland parity" and "foreign parity" are secured

Provision is made for mutual consultation if any party to the agreement feels aggrieved with the operation of customs regulations, quantitative restrictions, the observance of customs formalities, and the application of sanitary laws and regulations for the protection of human, animal, or plant life The customs regulations and formalities have been a common source of friction, particularly since the depression The sanitary regulations are frequently used to escape from the obligations of the Most-Favoured-Nation Clause The provision for mutual consultation, laid down in the trade agreements limits the arbitary use of these measures

Tenure of the Agreements—The usual tenure of the trade agreements is three years, and if not then terminated on six months' notice, will continue in effect until six months' notice of termination is given An agreement may, however, be terminated within the initial period in the case of an infringement of the most-favoured nation obligation, or the adoption of policies which tend to impair or nullify the advantages accruing under the agreement, or a wide variation in the rates of exchange between the currencies of contracting countries, etc

From the foregoing analysis of American commercial

policy it will be seen that the United States has given a valuable lead in the direction of reduction of trade barriers The abandonment of the single column, autonomous tariff system is significant This step gives recognition to the principle that the height of domestic tariffs may create international friction The tariff retaliation which followed the placing on the statute book of the Hawley-Smoot Tariff Act of 1930 brought home this elementary truth to the American people A moderate protective tariff, determined by the reasonable economic requirements of a country, may be regarded as a purely domestic concern of the country levying it and would not give sufficient cause to foreign countries to resort to retaliation in self-defence. A moderate tariff, is undoubtedly, of purely domestic concern But when the tariff is raised beyond this reasonable limit it must cause international complications Hence the need for tariff bargaining has been felt to keep down the general level of tariffs America has adopted the traditional European tariff bargaining system The danger of securing special exclusive preferences has also been recognised and therefore the new American trade agreement policy is based on the principle of equality of treatment

In view of the present international economic conditions, the American reciprocal trade policy may be said to have secured valuable reductions in trade barriers [1] Tariffs have

been reduced, though the reductions are moderate The principle of equality of treatment has also been enforced in regulating trade barriers In this direction, however, as we have shown above, the United States has tried to secure discriminatory advantages in certain cases [1] Besides, the principle of Imperial Preference is also recognised and respected This is another grave defect, though the United States is not alone to blame for this Discriminatory practices must be completely discarded in the interests of international economic rehabilitation Economic imperialism has dangerous political implications and is the *root cause of modern international political instability.* General public opinion must be created, by disseminating information and taken into confidence in checking the callous vested interests The United States should give a bold lead to the world by extending whole hearted support to the cause of equality of treatment Discrimination should be removed in toto, and the use of import quotas export subsidies, etc, given up In this way alone can the essential flow of international trade be re established President Roosevelt's move towards a liberal commercial policy needs to be strengthened.

We may now tabulate our conclusions

(1) America has fortunately abandoned the principle of tariff autonomy in formulating and moulding her commercial policy in favour of the traditional European tariff bargaining system

(2) The principle of equality of treatment is the accepted guide of the American commercial policy

(3) Valuable reductions in trade barriers have been secured with the aid of reciprocal trade agreements. But the barriers are still very high Reductions hitherto secured are moderate A more vigorous drive is, therefore, needed. In this direction however, much will depend upon the co-operation of other countries, particularly Britain and France, with the United States

(4) Substantial equality of treatment has been secured through the reciprocal trade agreements programme But the vested interests created by the discriminatory practices are strongly entrenched and it seems to be very difficult to dislodge them ot their vantage ground Concerted and vigorous efforts ought to be made to cure the body-politic of this chronic disease, if the economic and social structure of the world is to be saved. To secure economic and political stability, essential for the expansion of world trade, economic imperialism as an instrument of commercial policy for obtaining exclusive preferences, must be discarded, and the backward countries should be given sufficient help to secure efficient and economic utilisation of their resources

CHAPTER VIII

OTTAWA TRADE AGREEMENTS

***Economic Imperialism*—ECONOMIC** Imperialism constitutes the most serious menace to world security The policy of the open door is at best a mere palliative The Treaty of Versailles created new economic problems Germany was deprived of its colonies and they were redistributed The economic independence of Dominions colonies dependencies and mandated territories varies considerably from complete dependence to virtually full independence Even in the case of Dominions having full independence like Canada Australia New Zealand South Africa etc the mother country derives substantial economic and political advantages These economic and political advantages have offered a strong temptation to an aggressor The future of world economic development will therefore rest upon a proper and just solution of this great problem So long as colonies are a source of profit and a gem in the Crown the struggle between the haves and have nots must continue The spoils will be shared according to the strength of the parties In this chapter therefore we propose to analyse the trade agreements Britain entered into with her Dominions which have full fiscal independence in 1932 and the exclusive economic concessions she obtained thereunder

Relapse in British Fiscal Policy—That Britain discarded her traditional policy of free trade under the stress of trade depression has already been shown it was a triumph for the conservatives The protectionists argued that Great Britain must have a tariff as a means of defence against the aggressive protectionist policies pursued by other countries Mr Baldwin agreed that high tariffs are a great bar to the growth of trade and commerce but he argued that

Britain would use the protectionist system she intended to build up to pull down the tariffs of the world.[1]

The Import Duties Act of 1932.—By the Import Duties Act of 1932, Britain adopted an extensive protectionist system. The credit rests with Mr Neville Chamberlain for having brought to fruition the dream of his father Joseph Chamberlain. The main features of the policy as outlined by Mr Chamberlain are as follows Firstly, that an *ad valorem* duty of 10 per cent shall be imposed on all goods imported into the United Kingdom, with the exception of goods already dutiable and those specially excepted. Among the goods specially excepted are wheat, meat, bacon, raw wool, raw cotton, etc [2] Secondly, the establishment of a committee "for the purpose of giving advice and assistance to the Treasury "[3] This committee is empowered to recommend additional duties on imported goods which appear "to be either articles of luxury or articles of a kind which are being produced, or likely within a reasonable time to be produced, in the United Kingdom, in quantities which are substantial in relation to the United Kingdom consumption" The Treasury may on the receipt of such recommendations levy a duty directly by an order Thirdly, the Board of Trade is empowered to levy retaliatory duties up to 100 per cent, over and above other duties already imposed, on goods coming from any country which discriminates against exports from the United Kingdom. Fourthly, the orders imposing new duties issued by the Treasury or the Board of Trade shall expire unless ratified by the Parliament within twenty eight days Thus, Britain has

definitely discarded free trade and taken to protection[1] Lord Snowden characterised this policy as disastrous to the British economic life and prosperity The Import Duties Act and the Permanent Advisory Committee set up under it enabled the vested interests to build up a strong protectionist system at the cost of the general taxpayer Subsequent events have falsified the claims of those who supported the Act as a temporary measure It is no longer a measure of 'slimming ' At the very commencement of its work the Import Duties Advisory Committee proposed the fixing of *uniform additional duties of 10 per cent ad valorem* increasing thereby the duty on manufactured articles to 20 per cent The duties on luxuries and other articles were raised still higher In short the tariffs on British imports were substantially raised and have remained high since then

Ottawa Trade Agreements—Having built up an extensive protectionist system under which she could offer a wide range of preferences to the Dominions and the Colonies the British Government called a Conference of the Empire countries at Ottawa in August 1932 to negotiate separate preferential trade agreements Mr Baldwin explaining the aims of the Conference stated that the fundamental objective 'should be to clear out the channels of trade among ourselves There are two ways in which increased preferences can be given either by lowering barriers among ourselves or by raising them against others The choice between these must be governed largely by local considerations but subject to that it seems to us that we should endeavour to follow the first rather than the second course For however great our resources we cannot isolate ourselves from the world He added It is necessary to bear in mind that the percentage of duty charged on the value of the article is of great importance in assessing the

value of a prefeernce A preferential rate of duty, if the preference is to be of material assistance, must not be so higb as, in effect, seriously to restrict importation [1] and the United Kingdom delegation would urge upon tbe Dominions that the rates of duty charged should be so graduated as to give the products of the United Kingdom a reasonable chance of competing on equal terms, and that the rate of duty against United Kingdom products should be fixed for protective purposes no higher than is necessary to give a reasonably efficient industry in the Dominion a fair chance"

Aim of British Policy—Thus, the British objective as outlined by Mr Baldwin, in negotiating the Ottawa trade agreements was threefold First, the establishment of exclusive preferential treatment of trade within the Empire Secondly, preferencial treatment to be accorded by lowering trade barriers against the movement of goods with the Empire Thirdly, the preferential rate of duty was expected to be such as not to seriously restrict the flow of trade The British Government realised that the increase in tariffs on imports would restrict the flow of British exports and raise the cost of living Therefore, the Ottawa trade agreements are intended to provide additional markets within the Empire for British goods Thus, an attempt has been made to exclude foreign goods from Empire markets It should be noted that in a large number of cases British and Dominion industries are at present non competitive In such cases, the exclusion of foreign goods from Empire markets, by preferential tariff in favour of Britain, would enable British industrialists to capture the market in the Dominions Where British industries compete with Dominion industries, the Dominions would be expected to mould their tariff policy in such wise as to give British goods 'a reasonable chance of competing on equal terms' Further,

Dominion tariffs are expected to protect only those industries which are reasonably efficient and the nature of protection would be such as to offer them just a 'fair chance'.

Thus, Mr Baldwin wanted to keep up British industrial supremacy under the shelter of Imperial preference No longer able to face the open competition of the well-organised and efficient European, American and Japanese manufacturers, British industralists thought of resorting to this artificial and uneconomic diversion of trade The structure of British industries required a radical reconstruction, instead of a dose of protection Mr Baldwin's objective of putting a premium on British industrial inefficiency, under the Ottawa trade agreements, would fail to provide a sound economic basis for the British industrial system Further, Mr Baldwin intended to fetter the fiscal policy of the Dominions without putting any corresponding check upon British protectionism This does not sound equitable The Dominions are expected to protect only 'reasonably efficient' industries when Britain protects her beet sugar industry, which, according to her own experts can never face open competition

The Economist[1] suggested three important principles as a guide to the British commercial policy at Ottawa, in the interests of British trade and industries (1) The essence of any bargain must be a drastic lowering of tariff schedules A widening of British preferences unaccompanied by substantial reductions in general tariff rates in unacceptable (2) No agreement must be signed which would so far tie Britain's hands as to ruin her chance of successful bargaining in forthcoming negotiations for lower tariffs in the European zone Any forward fiscal move at Ottawa must be complementary to and not exclusive of future agreements between Britain and her chief foreign customers (3) Britain cannot afford to make any concessions which would have the effect of raising substantially the cost of living and the cost of production in Great Britain

1 Vide 13 8-1932 p 290

It does not come as a surprise if these principles could not be followed in practice by the British delegates while negotiating trade agreements at Ottawa. The reasons are obvious Britain expected the Dominions to offer "concessions of a really far-reaching character" on "basic British exports" by "a drastic lowering of tariff schedules" while she was not prepared to offer similar concessions to the Dominion produce in the British market lest it should "have the effect of raising substantially the cost of living and cost of production."[1] The inconsistency of this attitude becomes obvious when we recall that Dominion tariffs were essentially moderate, determined by the reasonable requirements of domestic industries and finance The scope, therefore, for any substantial reduction in these schedules was limited. Reduction in Dominion tariffs would in many cases, have been a real sacrifice on the part of the Dominions, for the change would have had immediate repercussions on their trade and industries In return for these valuable concessions, Britain was prepared to give such concessions, without any binding as would not affect materially the British costs, and enable her to continue tariff bargaining in the European markets In the face of the most uneconomic protectionist system in Britain, it was quite natural if the Dominions refused to agree to these principles. By her tariff policy Britain had unequivocally pledged herself to protection and the hope of freer trade within the Empire was just a mirage The dream of a grand Imperial Zollverein, with the present structure of British industries and the policy of economic self sufficiency which Britain adopted in 1931, is very difficult to realise in practice The future promises rapid industrialisation of backward areas, in the interests of their nationals In view of these facts, the British conception of Imperial economic unity, as outlined by Mr Baldwin and his supporters, is an

anachronism The ideal of Imperial Zollverein[1] would became economically more practicable if Britain moulds her policy of agricultural protection, and accepted the principle that the *British industries should be complementary to Dominion industries*, particularly in those cases where the Dominions can build up more efficient industries Radical changes in the present structure of British industries are inevitable, British industrialists have now to prove their adaptability The lesson which the Dominions could take from the recent developments in British fiscal policy is to raise their tariffs schedules in favour of domestic producers

Structure of the Ottawa Trade Agreements:

Dominion Fiscal Policy Regulated—Let us now analyse the structure of trade agreements entered into at Ottawa *Great Britain entered into separate trade agreements with* Australia, Canada, Newfoundland New Zealand, South Africa, Southern Rhodesia and India The most important feature of these trade agreements is the pledge which Britain secured from the Dominions in matters of tariff policy affecting British goods imported by them The agreements provide that protection by tariff shall be afforded only to those industries which are "reasonably assured of opportunities of success"[2] *During the currency of the* agreements the tariffs imposed by the Dominions shall be based on the principle that protective duties shall give full opportunity of reasonable competition on the basis of the relative cost of economical and efficient production, provided that in the application of such principle special consideration may be given to the case of industries not fully established Further *no new protective duty shall be imposed* and no existing duty shall be increased on British goods in excess of the recommendations of the tariff board[3] The

British producers were given full rights of audience before the tariff board.

These provisions are to be found in the trade agreements with Australia Canada, and New Zealand The Indian trade agreement in this respect, is of a special type, as will be shown in a subsequent chapter[1] From the foregoing provisions it will be seen that the British Government got valuable undertakings from the Dominions which would prevent them from adopting a policy of economic self-sufficiency of which Britain was shrewdly suspicious But the pledges were obviously one-sided for Britain in return has given no such general guarantees

Difficulties arose in the application of this new policy The interpretation of these provisions by the tariff boards of the Dominions was not quite suitable to British interests Definite precise and reliable information about the relative costs of production of a given article in the two countries could not be easily secured Besides the possibility of substitution cannot be ignored in such cases This widens the scope of tariff board enquiry and adds to the difficulties. The question of costs is a very delicate one, the information is invariably a closely guarded secret Again the task of sitting in judgment over the two sets of data of costs is much more difficult the material collected has to be carefully sifted and scrutinised giving the benefit of doubt to the domestic industries These difficulties have been indicated by the Canadian tariff board In view of the vital national interests at stake, the interpretation of the pledges had to be liberal The Australian tariff board refused to put a strict interpretation upon these undertakings They declared that a fine adjustment of duties so as to place efficient manufacturers of the United Kingdom and of Australia on exactly the same price-level in the Australian market would seriously dislocate Australian industries There is no hard and fast formula which can be used with any degree of satisfaction, and the problem of reasonably interpreting

the agreement involves much more than an arithmetical calculation of the difference between the costs in the United Kingdom and in Australia Each case must be considered on its merits and judgment given after a close examination of all available relevant facts Similarly the New Zealand Commission held that all that Britain is entitled to under the agreement is a fair deal as understood by a reasonable and fair minded man

Further the British Government is given the right to request the Dominion Governments to get their existing duties reviewed by the tariff boards in the light of the aforesaid undertakings given by them For instance the Canadian Trade Agreement provides as follows —[1]

His Majesty s Government in Canada undertake that on the the request of His Majesty s Government in the United Kingdom they shall cause a review to be made by the Tariff Board as soon as practicable of the duties charged on any commodities specified in such request in accordance with the principles laid down in Article II hereof and that after the receipt of the Report of the Tariff Board thereon such Report shall be laid before the Parliament and the Parliament shall be invited to vary wherever necessary the tariff on such commodities of the United Kingdom origin in such manner as to give effect to such principles

Similarly the Australian Trade Agreement contains the following undertaking [2]

His Majesty s Government in the Commonwealth of Australia undertake that a review shall be made as soon as practicable by the Australian Tariff Board of the existing protective duties *in accordance with the principles laid down in Article hereof* and that after the receipt of the report and recommendation of the Tariff Board the Commonwealth Parliament shall be invited to vary whenever necessary the tariffs on the goods of United Kingdom origin in such manner as to give effect to such principles

New Zealand gives a similar pledge [3]

These pledges notwithstanding the difference as regards interpretation in their enforcement have given tangible

assistance to the British trade and industries in keeping and strengthening their hold on the markets of the Dominions If in certain cases the British interests have felt dissatisfied with the attitude taken up by the tariff boards in some of the Dominions, it is due to the conflict between the British and domestic interests, in which the latter have naturally been preferred. Besides, the inherent difficulties of the situation are also partly responsible for the misunderstanding created in certain quarters The problem of determining relative costs is both difficult and delicate The decisions, therefore, are apt to cause dissatisfaction

Administrative Protectionism.—The agreements provide for the proper regulation of customs administration in order to check the growth of administrative protectionism For instance, the Agreement with Canada provides that the customs administration in Canada shall be governed by such general principles as will ensure (a) the avoidance, so far as reasonably possible, of uncertainty as to the amount of customs duties and other fiscal imposts payable on the arrival of goods in Canada, (b) the avoidance of delay and friction to a minimum, and (c) the provision of machinery for the prompt and impartial settlement of disputes in matters appertaining to the application of tariffs[1] The Canadian tariff board has adopted an extremely judicious attitude in the interpretation of the guarantees extended under the trade agreement Unwarranted delays, needless and vexatious formalities, and other administrative difficulties have been minimised. The simplification of customs formalities, prompt and speedy clearance of goods, and stability in tariff treatment constitute a distinct contribution towards the improvement of commercial relations between the Empire countries To this extent the Ottawa trade agreements mark a step in the direction of free trade They give a valuable guarantee against the growth of restrictions in future Though limited in scope, these provisions show the futility of the wasteful restrictive practices which fetter the movement of trade These undertakings

1 Vide Art. 14

show the directions in which future commercial policy for securing freer world trade should move

Similarly, the Agreement with Australia[1] provides that the Australian government undertake to repeal as soon as practicable the prohibition imposed on the import of certain goods, remove the surcharges, and reduce or remove the primage duty on British goods imported into the country In accordance with this undertaking the Australian Government reduced the surtax[2] on a number of commodities with effect from September 2 1932 Among the articles thus affected are piece-goods artificial flowers, apparel, umbrellas, paints varnishes, leather manufactures, manufactured stationary, hair and cloth brushes, straw envelopes, etc[3] Similarly, the prohibition of importation into Australia of certain goods, which had been in force since April 4, 1930, was removed with effect from August 31, 1932 The articles covered are, cheese lemons, oranges, dried fruits, fruits preserved in liquid vegetable jams and jellies, pickles, sauces, chutneys batteries and accumulators of certain kinds, wireless receiving sets partly or wholly assembled, aluminium ware other than spoons and forks, tiles, sanitary and lavatory articles of earthenware and enamelled fireclay, matches, iron and steel beams, channels girders, etc[4] The primage duty was removed on the following articles with effect from September, 2, 1932 barbed wire, wire netting, agricultural machinery and implements, chaff cutters and horse gears, churns of all kinds, strippers, etc[5] In the detailed list of the articles on which primage duty is thus removed the different types of agricultural machinery are very prominent

Tariff Preferences Granted by the Dominions—In addition to the definite assurances accorded affecting the course of tariff policy, the Dominions extended valuable

tariff preferences on British imports For instance, the Canadian agreement provides [1]

> "His Majesty's Government in Canada will invite Parliament to pass the legislation necessary to substitute for the duties of customs now leviable on the goods specified in Schedule 'E' the duties shown in that Schedule provided that nothing in this Article shall preclude His Majesty's Government in Canada from reducing the duties specified in the said schedule so long as the margin of British preference shown in that schedule is preserved or from increasing the rates under the intermediate or general tariff set out in the said Schedule"

This undertaking introduces two important principles in the Canadian tariff policy The more important British imports into Canada, specified in Schedule 'E are to be accorded preferential tariff treatment over similar articles imported from other countries. Secondly the margin of British preference, specified in the said schedule is to be preserved. This clause perpetuates commercial discrimination The result is that the power of the Government of Canada of reducing tariff duties is definitely fettered, the margin of preference has to be maintained. The Government of Canada therefore cannot negotiate commercial treaties with foreign countries for a substantial reduction of trade barriers as her ability to offer reciprocal concessions is limited. Above all she has resorted to discrimination. Thus both the bargaining capacity of the Canadian Government and the prospects of a freer world trade are limited. Further, it is interesting to note that the agreement leaves full latitude for fresh restrictive measures on non British goods The Canadian Government has unfettered right to increase the duties set out in the intermediate and general tariffs In short the Ottawa System introduced the dangerous principle of tariff discrimination, extended its scope and consolidated it by fettering the hands of the Dominions against change Subsequent events have unequivocally demonstrated the dangers inherent in tariff discrimination practised on such a wide scale The growth of new methods of trade restriction is in no small measure

1. Vide Art. 9

due to the exclusive and discriminatory character of the Ottawa System The political problem of colonies,[1] markets, raw materials, etc, with which the world is faced today has to a large extent been created and considerably complicated by this network of discrimination Britain, therefore, cannot lightly escape the blame for the present economic and political chaos the world has fallen in

The Australian agreement contains similar undertakings with slight variations The agreement provides [2]

"His Majesty's Government in the Commonwealth of Australia will invite Parliament to pass the legislation making the tariff changes necessary to give effect to the preference formula set forth in Part I of Schedule F" appended hereto subject to the exceptions indicated in Part II of the Schedule, and further undertake that existing preferential margins which exceed those laid down in this formula shall be maintained subject, however, to the right of His Majesty's Government in the Commonwealth of Australia to reduce the existing margins of preference in the case of goods of the kind specified in Part III of that Schedule to an extent not exceeding the amounts shown therein"

Thus, the margin of preference is stabilised and the scope for general reduction of tariff barriers restricted The agreements with Newfoundland,[3] New Zealand,[4] South Africa,[5] and Southern Rhodesia,[6] also contain provision consolidating the margin of tariff preferences In this rigidity of the preference margin lay the seed of economic strife

Australian Tariff Preferences.—These rigid tariff preferences have presented a very strong barrier to trade with the non-Empire countries, their effects can be adequately gauged on detailed analysis of the articles contained in the schedules attached to the texts of the agreements The Australian schedule contains a very wide range of com-

modities over which tariff preferences granted to the United Kingdom have been substantially increased.[1] In this connection it is interesting to note that Australia, before the Ottawa agreement extended tariff preferences on a large number of British articles Under the agreement the margin of preference has been increased, by raising the general tariff, and its scope widened with the inclusion of new articles The general tariff has been raised on a large number of commodities. Normally the increase in the *ad valorem* duties of the general tariff varies up to 15 per cent.[3] From this extensive list it is clear that the Australian agreement has increased the tariff barriers against non Empire trade At this stage however it needs to be noted that the tariffs on the British goods imported into Australia have been lowered on a few articles.[4] To a very limited extent, therefore the agreement has reduced the trade barriers and helped thereby the growth of trade within the Empire The following table gives a more definite idea of the nature of tariff reductions accorded by the Australian Government on British goods imported into Australia.

Articles	British Preferential Tariff	
	New	Old
Rum	37s.	40s.
Blended rum	37s.	41s
Tobacco unstemmed	2s	2s. 6d
Tobacco stemmed	2s 6d.	3s
Cigars	18s	20s
Cocoa butter	1d.	1½d.
Petroleum	2½d.	2d.

1 The tariff preferences, subject to certain exceptions, are determined with the following formula :—

(a) when the British goods are free of duty or liable to duties not exceeding 19 per cent. ad valorem the difference between the British preferential rate and the rate upon similar goods from the most-favoured-nation country shall be at least 15 per cent. ad valorem.

(b) when the British goods are liable to duties exceeding 19 per cent. ad valorem, and not exceeding 29 per cent. ad valorem, the difference between the British preferential rate and the rate upon similar goods from the most-favoured-nation country shall be at least 17½ per cent. ad valorem.

(c) when the British goods are liable to customs duties exceeding 29 per cent. ad valorem, the difference between the British preferential rate and the rate upon similar goods from the most-favoured-nation country shall be at least 20 per cent. ad valorem, provided that in no case shall this margin be applied so as to result in a rate of duty exceeding 75 per cent. ad valorem.

2. Vide B T J., 20-10-1932, pp. 545-60

3. Ibid. There are few cases in which the duties have been raised higher.

4. Ibid.

Thus, the reduction in duties is limited to a very few articles, whereas the increase in general tariff covers an extensive list of commodities In effect, definite attempts have been made to divert the non-Empire trade to Empire countries

The Canadian Tariff Changes—Canada, unlike Australia, has a triple-line tariff Schedule 'E', attached to the Canadian agreement referred to above, sets forth 220 items of the Canadian tariff in respect of which new or increased margins of preferences were granted by Canada to the United Kingdom The schedule covers a very wide range of commodities, and includes, inter alia, a large number of items previously dutiable at the British preferential rate which are now transferred to the free list As for the rest the British margin of preference has been increased, in some cases by lowering the British preferential rates, and in others the intermediate and general rates have been increased to provide the agreed margin of preferences

A more detailed analysis of the schedule is essential for a proper understanding of the nature of tariff changes The free list has been considerably enlarged and the duty remissions effected thereby are substantial This increase of the items in the free list is a valuable contribution towards freer world trade Some of the most important articles are included in this free list, as can be seen from the following brief statement [1]

Article	Former Duty
Books	5%
Printed advertising matter	10 cents per lb
Roofings and shingles of saturated felt	15%
Blood Albumen	5%
Stearic Acid	$12\frac{1}{2}$%
Nitric Acid	15%
Sulphuric Acid	15%
Acid phosphate	$12\frac{1}{2}$%
Phospheric Acid	15%
Castile Soap	1 cent
Essential Oils	5%

Article	Former Duty
Earthenware tiles	25%
Asbestos	15%
Glass	17½%
Alluminium	15 to 30%
Bars of iron	5%
Sheets of iron and steel	7½%
Girder Rails	4 5 dol
Iron or steel angles	1 dol
Forgings of iron or steel	2%
Typewritees	10%
Machinery	15%
Engines for motor trucks, etc	15%
Motor cycles	12½%
Knives	20%
Electric telegraphic or telephonic apparatus	15%
Electric wireless or radio apparatus	15%
Electric storage batteries	15%
Electric switchgear, flame proof	15%
Steel bicycle rims	15%
Pig leather and morocco	15%
Leather tanned	15%
Indian Rubber boots and shoes	15%
Fertilisers	5%
Barytes	15%
Gasoline and Steam engines	15%

Further, the Government of Canada, under the agreement, has lowered British preferential tariff on a large number of commodities of different types This is a distinct contribution to the reduction of tariff barrier on world trade, particularly discriminatory tariffs The nature of tariff reductions in the preferential tariffs on the British imports into Canada can be seen from the following table

Reductions in Preferential Tariff on British Goods.[1]

Article	Rates of Duties	
	New	Old
Cigarettes	3 5 dol	4 10 dol
Cut tobacco	80 cts	95 cts
Manufactured tobacco	75 cts	90 cts
Ale, beer, port and stout	25 cts	30 cts
Fruit syrups and fruit juices	50%	17½%

1 Compiled from B. T J., 20-10-1932 pp. 561 70

Article	Rates of Duties New	Old
Ethyl alcohol	8 dol	10 dol
Spirits	8 dol	10 dol
Non alcoholic preparations	5%	15%
Perfumery	20%	25%
Type for printing	7½%	12½%
Wire	10%	15%
Axles of iron and steel	10%	20%
Ore crushers etc	7½%	10%
Ball and roller bearings	5%	15%
Table knives and forks	15%	20%
Spoons	15%	20%
Guns and rifles of certain kinds	5%	10%
Cotton woven fabrics	15%	22½%
Belting leather	12½%	15%
Caps hats coats cloaks etc of fur	15%	20%

From the detailed facts noted above it will be seen that Canada has offered substantial tariff concessions on British goods imported into Canada This is a welcome feature of the Canadian Agreement as it marks an important step in the direction of reduction of trade barriers This step is more significant as the Canadian tariff is relatively moderate But it is unfortunate to note that Canada has strengthened British preferences in a number of cases by raising the intermediate and general tariff The increase in rates is not restricted to a few articles of special importance to Britain, its scope is fairly wide and a large number of articles of different types are included The following table gives us some idea of the increased duties of the intermediate tariff [1]

Article	Rates of Duty New	Old
Butter	3 cts	2 cts
Florist stock	15%	Free
Fruit syrups and juices	25%	22½%
Chemical compounds	10%	Free
Aniline and coal tar dyes	10%	Free
Perfumery	40%	32½%
Surgical Dressings	25%	17½%
Gums	15%	Free
Cotton seed oil	10%	Free

Article	Rate of Duty New	Old
Tires of steel	10%	5%
Cream separators	25%	Free
Coal cutting machines	20%	Free
Printing presses, etc	10%	5%
Typewriters	25%	20%
Knives	30%	27½%
Surgical and dental instruments	10%	Free
Nitrate and Acetate of lead	10%	Free
Brass band instruments	30%	22½%
Caps hats etc of fur	30%	27½%
Hyposulphate of soda	10%	Free

From the foregoing table it will be seen that the duties in the intermediate tariff have been increased on a majority of the articles included in the schedule In addition to the articles enumerated in the foregoing table it may be noted that several chemicals which were on the free list before, are, under the agreement, subject to duties varying from 10 to 25 per cent Similarly, the intermediate tariff on iron and steel articles has also been raised The imports of textiles from non-Empire countries are also subject to higher duties

The general tariff, in certain cases is still higher than the intermediate tariff This means in practice, greater discrimination, particularly in favour of British goods The nature of discrimination can be adequately gauged by comparing the British preferential tariff with the intermediate and general tariffs The following table will give some idea of the tariff treatment accorded to goods imported into Canada from different sources

Customs Duties fixed under Schedule 'E'

Article	British preferential Tariff	Intermediate Tariff	General Tariff
Florist stock	Free	15%	20%
Potatoes	Free	Free	75%
Waxed stencil paper	10%	32½%	35%
Stearic acid	Free	17½%	20%
Muriatic acid	Free	22½%	25%
Printing ink	12½%	17½%	25%

Customs Duties fixed under Schedule 'E'

Article	British Preferential Tariff	Intermediate Tariff	General Tariff
Tiles	Free	32½%	35%
Type for printing	7½%	17½%	20%
Wire	10%	30%	35%
Ore crushers	7½%	20%	25%
Machinery	Free	27½%	35%
Table knives	15%	30%	35%
Motor cycles	Free	20%	30%

Such a discriminatory tariff treatment of non-Empire goods is apt to lead to retaliation

Tariff Preference Accorded by the Union of South Africa —The agreement provides that His Majesty's Government in the Union of South Africa will arrange to pass the legislation necessary to secure to British goods specified in Schedule E the margin of preference over similar foreign goods shown in the Schedule [1] The nature of preference can be gauged from the following table [2]

Margin of preferences

Commodity	Former margin	New margin
Coffee	Nil	1d per lb
Fish	¼d per lb	1¼d per lb
Meat	¼d per lb	¾d per lb
Cranes	Nil	7½%
Bucket conveyers	Nil	7%
Vacuum Cleaner electric	Nil	5%
Machinery	3%	5%
Batteries electric	5%	10%
Locomotives	Nil	5%
Sprayers and sprinklers	Nil	10%
Tractors	Nil	10%
Typewriters	Nil	10%
Radio apparatus	Nil	10%
Asphalt and bitumen	Nil	10%
Soap toilet	Nil	15%

The new margins of preference specified in the foregoing table were secured by raising the duties on foreign imports

on a large number of articles This Agreement has led to substantial increase in tariff barriers on non-Empire trade

New Zealand Extends Tariff Preference.—Under the trade agreement New Zealand agreed to accord tariff preference on certain categories of British imports and exempt them from surtaxes The New Zealand tariff has accordingly been amended and the surtax on British imports removed. It is interesting to note that the new margin of preference has been secured by reducing the British preferential as well as general tariffs[1] This is a welcome feature of the agreement The articles affected are confectionary, apparel and ready-made clothing, hosiery, silk and artificial silk piece-goods.[2]

Tariff Preferences Accorded by Southern Rhodesia.—Southern Rhodesia, under the agreement, agreed to extend the margin of preference for certain British goods[3] This preference has been secured by raising the tariffs[4] For instance, on electrical materials (except cable and wire), imported duty free from Britain before the agreement a duty of 5 per cent is levied, and those imported from foreign countries are charged 15 per cent Thus, the margin of preference for British goods is raised from 5 per cent to 10 per cent Similarly batteries, imported duty free from Britain before the agreement, are now subject to an import duty of 5 per cent The import duty on foreign batteries is raised from 5 to 20 per cent., to provide a preference margin of 15 per cent for British goods instead of 5 per cent The tariff treatment extended to other goods is of the same kind. Thus, tariffs have been raised and the margin of preference widened.

Tariff Preferences Granted by Newfoundland—Newfoundland agreed to grant a tariff preference of 10 per cent *ad valorem* on certain specified goods, subject to the right *of reducing the margin of preference if the grant of prefer-*

1 Vide B. T J., 10-10-1932 p 573.
2. Ibid, 13-10-1932 p 504
3. Vide, Art. 8.
4. For details, see B. T J., 20-10-1932, p. 572 and ?? 10-1932, p. 619

ence involved loss of revenue This protective clause was kept because Newfoundland depends largely upon customs tariff for revenue Any substantial fall in customs receipts would imperil the entire financial system of the country. Hence the reservation In the list large number of articles are included [1] The agreement accords a preference of 10 per cent on 61 classes of goods

Other Parts of the Empire—Another important feature of the agreements is the undertaking on the part of the Dominions to extend the preferential tariff to exports from the British Dependent Empire in return for an undertaking on the part of the United Kingdom to invite the Governments of the Colonies (except such are pledged to the Open Door by international agreement) to grant to the Dominions general preferential benefits and some specific preferences The general form of the undertaking is as follows·

> His Majesty's Government in the United Kingdom will invite the non-self governing Colonies and Protectorates to accord to any preference which may for the time being be accorded to any other part of the British Empire provided that this clause shall not extend to any preferences accorded by
> and further, will invite the Government of the Colonies and Protectorates shown in Schedule to accord new or additional preferences on the commodities and at the rates shown therein"

Thus, the former Open Door in the Colonial Empire was double-locked by the Ottawa Agreement [2] Henceforth the door can be opened only with the consent of the whole Empire It should be noted, however, that the policy of the Open Door in the Colonial Empire had already been abandoned before the Ottawa agreements What these agreements have done is to make the return to Open Door dependent on the consent of the Legislature of all units of the Empire instead of the British Parliament

Concessions Accorded by Britain.—*In* return for the concessions detailed above the United Kingdom agreed to

accord tariff preference to products imported from the Dominions In the first place, the British Government agreed to permit the entry of Dominions goods which were on the free list subject to certain reservations The reservations provide that as regards eggs, poultry, butter cheese and other milk products they will be permitted free entry for three years certain. After the expiration of three years the British Government reserves the right, if they consider it necessary in the interests of the domestic producers to review the basis of preference so far as it affects the aforesaid articles Further the British Government agreed to impose new duties on certain specified foreign goods The nature of articles covered under the agreements can be seen from the following table —

Article	Duty
Wheat in grain	2s per quarter
Butter	15s per cwt
Cheese	15% *ad valorem*
Apples raw	4s 6d. per cwt.
Pears, raw	4s. 6d. per cwt.
Apples, canned	3s 6d per cwt.
Other canned fruits	15% *ad valorem*
Dried fruits	10s 6d. per cwt.
Eggs, in shell	1s per great hundred.
	1s 6d per great hundred
	1s 9d per great hundred
Milk, condensed or sweetened	5s per cwt.
Milk, not sweetened	6s per cwt.
Milk, powdered	5s per cwt.
Honey	7s per cwt
Oranges raw	3s 6d. per cwt.
Grape fruit, raw	5s per lb
Grapes	1½d. per lb
Copper unwrought	2d. per lb
Cod liver oil	1s 4d per gallon
Salmon, chilled or frozen	1½d per lb
Peaches and nectarines raw	14s per cwt.
Plums raw	9s 4d. per cwt.
Maize flat white	10% *ad valorem*

The duties on the import of wheat, copper, lead and zinc into the United Kingdom are conditional on the Empire producers continuing to offer those commodities at prices

not exceeding the world prices. Thus, Britain does not want to pay higher prices and makes the Dominions believe that it is a great concession The imports of frozen mutton and lamb and frozen and chilled beef are subject to the following conditions· (1) Steps may be taken to raise the wholesale prices of frozen meat into the United Kingdom market to such a level as will maintain efficient production (2) To improve the situation, the British Government has a right to regulate the imports of meat into the United Kingdom (3) The policy of the British Government in relation to meat production, is, first, to secure the development of home production, and secondly, to give to the Dominions an expanding[1] share of imports into the United Kingdom (4) The Dominions must restrict their exports to the United Kingdom Further, in respect of bacon and ham, the British Government has agreed in the event of quantitative regulation of imports being enforced, to permit free entry for Canadian bacon and ham of good quality up to a maximum of 2,500 000 cwts per annum New Zealand has also agreed to quota restrictions on its exports of mutton, lamb and beef

Further, the British Government has undertaken to secure the margin of preference in the British market for certain dominion articles Under this agreement, Australian wine, not exceeding 27 degrees of proof spirit, is guaranteed a preference margin of 2s per gallon Similar preference is assured to wine imported from the Union of South Africa Coffee imported from Southern Rhodesia is given a preference margin of 9s 4d per cwt over foreign coffee[2] The margin of preference is also guaranteed for tobacco imported from Canada, Southern Rhodesia and South Africa With reference to tobacco the agreements provide as follows

His Majesty's Government in the United Kingdom will invite Parliament to pass legislation which will secure for a period of ten years from the date thereof to tobacco, consigned from any

part of the British Empire and grown produced or manufactured in Canada, (1) the existing margin of preference over foreign tobacco, so long, however, as the duty on foreign unmanufactured tobacco does not fall below 2s ½d per lb in which case the margin of preference shall be equal to the full duty

Another important concession granted by the British Government to the Dominions is not to reduce the general *ad valorem* duty of 10 per cent on certain specified foreign commodities imported into United Kingdom without the consent of the Dominions concerned This is an obstacle to the reduction of trade barriers against non-Empire trade

The variations in the terms of the agreements are to be effected by mutual consultation As regards the tenure of the agreements, it has been provided that they shall remain in force for a period of five years and if not denounced six months before the end of that period shall continue in force thereafter until a date six months after notice of denunciation has been given by either party

This is, in brief, the structure of the Trade Agreements Great Britain entered into with the Dominions at Ottawa It will be seen that the tariff barriers on non-Empire trade are higher under the Ottawa Agreements than those of the pre-Ottawa days Thus, the claim of Mr Baldwin that the Ottawa Agreements would "clear out the channels of trade" by "lowering barriers" is falsified Further, the scope for reduction in trade barriers, in future, is definitely restricted by undertakings given by the parties to the agreement

Commercial Discrimination.—The Ottawa Agreements have turned the dangerous practice of commercial discrimination, embodied in the ideology of Imperial Preference, into a well-knit system The economic and political repercussions of such a system must be far-reaching Such an agreement must result in an unwarranted and uneconomic diversion of trade[1] The damage caused to the normal flow of non-Empire trade must be serious,

1 "These arrangements, to which the most favoured-nation clause does not apply constitute so many obstructed arteries in the circulatory system of international trade." Vide S H Bailey "Economica," 1933 p 443.

since discriminatory tariff barriers put a very severe strain on competitive trade The concept of a closed and exclusive Imperial economic block[1] brought to fruition under the Ottawa Scheme has strengthened the claim for economic self-sufficiency and Imperial aggression Therefore the most valuable contribution towards economic disarmament and the improvement of international economic relations would be the abandonment of the practice of Imperial Preference It is necessary that all discriminatory commercial practices in international trade, irrespective of their garb must be penalised To start with Imperial Preference should cease to constitute an exception to the most-favoured nation treatment

The authors and advocates of Imperial Preference hoped that the Ottawa Agreements would facilitate the flow of trade within the Empire and increase thereby the purchasing power of the people They were expected to promote most efficient utilisation of the economic resources of the Empire and stimulate world trade In this connection it is essential to note the distinction between an increase in world trade and its diversion In the light of the preceding analysis of the structure of the agreements it is difficult to agree with the view that they would promote world trade or that they were really intended to do so Discrimination is an outstanding feature of the Ottawa Trade Agreements It is accepted that discrimination can never provide a sound basis essential for the development of world trade Per contra modern economic history shows us that discrimination is invariably a source of international ill feeling and friction Of course Imperial Preference is not a legal discrimination Legal validity however accorded to Imperial Preference under the Most-Favoured Nation Clause as an accepted exception does

improve the *de facto* situation, it continues to be a *de facto* discrimination, though not a *de jure* one It cannot be justified on economic grounds The spur of preference diverts the flow of competitive trade from the most economic channels to uneconomic ones With inevitable commercial retaliation the preference must curtail world trade and reduce, rather than increase the purchasing power of the people The increase in the purchasing power if any of the preferred countries is very costly and essentially temporary what is gained by the preferred countries is only a fraction of the loss sustained by the countries discriminated against It will lead to retaliation and trade war which must prove detrimental to both parties In short, discrimination and artificial diversion of trade can never add to the purchasing power of the people or increase world trade

Imperial Economic Blocks Different from Low Tariff Areas—The preferences accorded under the agreements are essentially exclusive and cannot be extended to foreign countries The scheme of a closed Imperial Economic Unit formulated by the Ottawa Agreements, is distinct and different from that of low tariff areas since the concessions accorded under the later scheme can be shared under certain circumstances by other countries as well The low tariff scheme, therefore, gives little cause for international ill-will and friction On the other hand, the parties to the Ottawa Agreements definitely stated "that it was their policy that no treaty obligations into which they might enter in the future should be allowed to interfere with any mutual preferences which Governments of the Commonwealth might decide to accord to each other, and that they would free themselves from existing treaties, if any, which might so interfere They would, in fact, take all steps necessary to implement and safeguard whatever preferences might be so accorded" Thus, the door was completely bolted against the foreign countries

This is not all. The obligations imposed upon the parties to the Ottawa Agreements, as will be seen from the preced-

ing analysis, have fettered their future course of commercial policy, they are no longer free agents in negotiating commercial treaties with foreign countries The specific margin of preferences should be maintained The scope for the reduction of trade barriers is therefore limited Piecemeal reductions, which alone can at best be had under the Ottawa commitments, can do little good *Per contra*, the tariff discrimination inherent in the Ottawa Agreements must lead to retaliation and add thereby to the trade barriers

Effects of the Ottawa Agreements on Empire Trade—A detailed statistical analysis of the working of these agreements is beyond the scope of the present chapter, which attempts merely to study the general tendencies of modern commercial policy Since the Ottawa agreements were concluded there has been a substantial growth in trade both within the Empire and outside A part of this expansion in trade is due to general economic recovery since the Ottawa Agreements which were concluded when the world was in the trough of depression There have been a number of other forces stimulating the growth of trade It is therefore difficult to demarcate precisely the effects of these agreements on the Empire trade

British Hold over the Empire Markets—It may be noted that the hold of Great Britain on the Empire markets has been considerably strengthened as a result of the exclusive tariff preferences accorded to her as may be seen from the following table

Import of British Goods
(in millions)

Year	Canada	Australia	New Zealand	Union of S Africa
	$	£ (stg)	£ (stg)	£
1930	162 6	54 2	20 2	29 7
1931	109 5	23 3	12 1	23 6
1932	93 5	17 4	11 4	15 1
1933	97 9	23 5	10 5	24 7
1934	113 4	25 1	12 6	32.3
1935	116 7	20 8	14 7	36 6
1936	123 0	33 8		
1937	147 3	38 8		

From the foregoing table it will be seen that since the Ottawa Agreements the imports of British goods into the Empire markets have increased rapidly Apart from other causes influencing the movement of trade, the effect of the Ottawa Agreements over British export industries has been two-fold In the first place, the agreements immediately checked the trend towards decline in British exports, which had definitely set in and was seriously menacing the structure of British industries It is essential to remember that British exports consist primarily of manufactured goods The rapid growth of industrial development, characteristic of the post-war economic conditions, was tending to restrict the market for British goods The backward countries had resorted to protection for fostering domestic industries, which was bound to check their import of British goods The principle of "compensatory tariff", incorporated in the Ottawa agreements themselves, was a clear indication of the determination on the part of even the members of the British Empire to develop their internal industries and place the interests of the domestic producers first and foremost The growing industries in the Dominions and other parts of the Empire were gradually replacing British goods in their domestic markets To this must be added the attempts made by foreign industries in competitive markets to capture the markets hitherto monopolised by British goods In this connection the competition offered by the Japanese manufacturers in the East since 1928 is very significant In fact, the Japanese goods have captured markets in competition with British goods both in the East and the West Japan is not the only competitor against British goods, though it is by far the most important This is just an illustration of the general industrial development of the post-war period Competition has been gradually growing Therefore, the effect of the Ottawa Trade Agreements in checking the decline of British imports in the Empire markets was an invaluable boon to the British industrialists The exports of British goods would otherwise have declined

Further the Ottawa Agreements have not merely checked the decline in the import of British goods in the Empire markets but they have definitely stimulated their expansion under the spur of an extensive scheme of tariff preferences British goods have been given tariff preferences since the beginning of the present century but it seems they were not adequate to enable them to keep their hold on the Empire markets It is evident therefore that under these circumstances the proper policy to be pursued was a radical readjustment and rationalisation of the structure of British industries so as to make them more efficient For instance if the Lancashire cotton industry with its long industrial experience and efficient labour supply cannot face open competition of the Japanese manufacturers the right course is to improve the structure of the industry Tariff preferences are apt to breed and perpetuate inefficiency

Britain has increased her hold on the Dominion markets under the stimulus of tariff preference as can be seen from the foregoing general review Economic recovery has also played an important part in stimulating the expansion of Empire trade The influence exerted by tariffs regulating the channels of trade will however be clarified by a detailed statistical analysis of the more important commodities By way of an illustration therefore a few Canadian imports will be examined Canada is a typical representative market of the Empire and the general trends revealed by the study of Canadian market can be safely applied to the other parts of the Empire

Britain Captures Canadian Market—It has already been shown that under the Canadian Agreement import duties on a large number of British goods were substantially reduced and in several other cases the intermediate and general tariffs were raised to provide a greater margin of preference Under this agreement British exports to Canada have increased as will be seen from the following table —

British imports into Canada for consumption
(In $-000)

Year	Animals & their products	Fibre Textile	Iron & its products	Non-ferrous metals	Non-metallic minerals	Chemical & allied products
1932	2,520	27,181	12,584	3 650	12,277	4,719
1933	2,779	30,987	15,805	2 818	13,262	5,294
1934	3 212	37,269	18,684	4 071	13,255	6,165
1935	3 533	39 361	20 407	6,000	12,690	6 331
1936	4,274	44,163	21 688	5 572	12,794	6,802
1937	6,115	52,643	29,794	7,302	13 300	7,858

Agricultural Implements and Machinery —That there has been a substantial increase in the import of British goods can be seen from the foregoing table It is, however, essential to analyse these statistics in greater detail in order to understand the effects of the trade agreement on more important commodities Let us take iron and its products In this general group agricultural implements and machinery are important The Canadian agricultural[1] implement industry has gradually improved its position and the efficiency of the machines manufactured in Canada has recorded marked improvement The fortunes of this industry are dependent upon the general farming situation During the depression, there was a definite turn-over from tractors back to horses That tendency has fortunately been reversed and the sales of machinery have increased Notwithstanding the improvement of the domestic industry, Canada continues to import farm implements and machinery The United States of America supplies the greater proportion of the Canadian requirements Due to the Ottawa Agreement, however, the United Kingdom has also been able to share the market, and her share is increasing In 1936-37 the imports from United Kingdom amounted to $263,160 and rose to $639 048 in 1937-38 Cream Separators and farm traction-engines are the principal items of agricultural machinery exported by the U.K Here it is interesting to note that Sweden has suffered most from the tariff

1 Vide Bruce, A. B : "Economic and commercial conditions in Canada " Appendix IV, p 114

preference accorded to the U K as competitive supplier to the Canadian market The share of Sweden declined from \$288 843 in 1936 37 to \$275 339 in 1937 38 The U S A has also suffered The imports of farm traction engines from Britain have increased from \$47 407 in 1936 37 to \$74 694 in 1937 38 The U S A supplies the largest proportion of the Canadian requirements and feels most the tariff discrimi nation in favour of the U K accorded under the Ottawa Agreement

Iron and Steel Castings and Forgings.—In the supply of iron and steel castings and forgings to the Canadian market the United Kingdom has a share The tariff preference has strengthened the hold of British manufacturers In this class of commodities the United Kingdom supplies forgings of iron and steel pressed steel wheels for use on railway rolling stock steel wheels and tyres of steel The imports of forging from United Kingdom have increased from \$76 510 in 1936 37 to \$134 979 in 1937 38 The United Kingdom is the largest supplier of this article the U S A being a poor second The imports of British steel tyres have increased from \$355 197 in 1936-37 to \$357 416 in 1937 38 The tariff preference has been very useful to this class of goods The preference puts the U S.A manufac turers at a great disadvantage

Imports of Cutlery—In the Cutlery group table knives forks and spoons are given tariff preference British imports of these goods have therefore increased The imports of steel table knives and forks increased from \$136 351 in 1936 37 to \$145 301 in 1937 38 The imports of British spoons rose from \$5 909 in 1936 37 to \$9 411 in 1937 38 The imports from the U S A have declined Germany and Japan are also important competitors in the market The domestic industry is equally important

Engines and Boilers—The imports of engines and boilers from the U K increased from \$317 thousand in 1932 to \$1 484 thousand in 1937 38 The U S A is the major supplier of this class of goods to Canada her exports in 1937 38 being

about \$8 million. The largest single item in this group is automobile and motor vehicle engines The United States of America supplies practically the whole of the automobile engine imports and the U.K. finds it very difficult to compete because the Canadian motor car manufacturing industry is almost a branch of the U.S.A. industry[1] Further, the U.K. manufacturers find it difficult to compete in prices with the light high speed diesel engines manufactured in the U.S.A. with horse power ranging from 80 to 100 With the increase in the demand for aircraft the imports of aircraft engines both from the U.K. and the U.S.A. is likely to rise Boilers are also largely supplied by the U.S.A. In 1937-38 Canada imported boilers valued at \$344 989 of which imports from the U.S.A. amounted to \$337 699 and those from the U.K. \$5 985

Mining and Metallurgical Machinery.—In view of the growth in the Canadian mining industry the demand for mining and metallurgical machinery has increased considerably in recent years The total imports into Canada have risen to \$6 7m in 1937-38 Of this the supplies from U.S.A. are valued at about \$6m. The share of U.K. has increased from \$418 thousand in 1932 to \$633 thousand in 1937 The increase in the British exports is partly due to the tariff preference It is significant to note that the U.S.A. continues her hold upon the Canadian market in spite of the discrimination.

Rolling Mill Products.—British rolling mill products also have captured a substantial part of the Canadian market With economic recovery the market expanded so that a part of the increase in the imports of British manufactures was due to the general recovery of trade the Canadian demand for these products rose from \$31m. in 1936-37 to \$43m. in 1937-38 The U.S.A. supplies the greater part of the demand For instance of the total imports valued at \$43m. in 1937-38 the U.S.A. supplies about \$24m. The U.K. stands second. The imports from the U.K. have risen

1. Vide Bruce, A. R., p. 8

from $6₂m in 1938 to $17m in 1937 38 In this group one finds that Britain s hold over the Canadian market is limited to certain classes of articles For instance imports of bars hot rolled bars plates galvanised sheets sheets for galvanising other sheets and band and hoop of iron or steel from U K have increased The tariff preference has rendered invaluable help to the British manufacturers in capturing the Canadian market The American manufac turers feel most the handicap of this tariff preference

Textile Machinery—The imports of British textile machinery have increased substantially In 1937 38 Britain doubled her exports of textile machinery to Canada over that of the previous year The exports of the U K rose from $468 000 in 1932 to $1m in 1937 38 But the U S A ranks first as supplier of textile machinery to Canada The U S A exports to Canada amounted to $3 572 129 in 1937 38 as against $1 155 170 exported by the U K The American predominance over the Canadian market is partly due to the fact that the mechanical equipment of the industry in both the countries is similar The British manufacturers are trying to adjust their production to suit the Canadian requirements[1] so that in future they may capture a part of the market hitherto supplied by the U S A

Imports of Pipes and Tubes—The domestic Canadian industry produces iron and steel pipes and tubes but the total output is not sufficient to meet the domestic demand In 1937 38 the total imports of tubes pipes and fittings amounted to about $2 55m The U S A is a major supplier of this class of goods In 1937 38 the U S A supplied goods worth $1 78m The British share has increased under the Ottawa Agreement In 1937 38 British imports were valued at $663 095

Imports of Vehicles—The total Canadian imports of vehicles in 1937 38 were valued at $47 3m Of this U K supplied $1 4m and the U S A $45 8m The imports of passenger automobiles were valued at $13m The U S A

1 Vide A R Brice p 101

shown sufficient adaptability and enterprise in catering for the demand[1] In future, therefore, the U K manufacturers will have to change their traditional policy lest they should lose their hold over the Canadian market

Non-Metallic Minerals—In the group of non-metallic minerals and their products the imports of certain British products have increased, particularly those enjoying tariff preferences For instance, the imports of asbestos products rose to $401,040 in 1937-38 It may be noted that Canada is a substantial producer of asbestos products and the market is highly competitive Britain is a principal supplier of tableware and her share increased to $3 38m in 1937-38 The imports of glass and glassware from Canada rose to $1 43m in 1936-37 In the following year 1937-38, however, the imports fell to $1,39m

Agricultural and Vegetable Products—In the group of agricultural and vegetable products which have received tariff preferences the United Kingdom has improved her hold over the Canadian market For instance, the imports of British cocoa butter have increased from 107 thousand lbs in 1933 34 to 1 689 thousand lbs in 1937 During the same period the imports from the U S A have declined from 1 661 thousand lbs to 8 thousand lbs Thus, Britain has captured the Canadian market and ousted the foreign competitors particularly the U S A This is a conspicuous case of trade diversion

Textiles—In the group of fibres textiles and textile products preferences tariff have rendered invaluable assistance to the British manufacturers The imports of artificial silk piece-goods from the U K have increased from $469,517 in 1935-36 to $954 035 in 1936-37 and $1,186 390 in 1937-38 Canada has an extensive domestic industry which checks the flood of imports The U K is a principal external supplier of artificial silk yarn and the imports of British yarn have risen to $893 425 in 1937-38 The tariff preference has also helped the British cotton industry The imports

[1] *Vide*, A R Bruce p 106

of unbleached fabrics from the U.K. rose to \$3 9m. in 1937-38 In respect of bleached and mercerised fabrics the domestic industry offers keen competition The Canadian cotton manufacturing industry is gradually improving its efficiency, so that the scope for foreign imports is limited. The imports of cotton yarn from U K increased to \$2 8m. in 1937-38 Here it may be noted that the imports from U.K. consist primarily of yarn of fine quality

Britain holds a predominant position as supplier of woollen piece-goods to Canada The gray wollen fabrics, flannels, over-coatings, tweeds, worsteds and serges, etc, are supplied almost entirely by the U.K. Tariff preferences have been invaluable in this branch of the trade

The Canadian mills offer severe competition in cheaper fabrics, for Canada is largely "a price market" Mr Bruce rightly remarks Canadian and U K mills are in competition in this market in practically the entire range of cloths, but the competition from the domestic industry is most severe in the lower and medium qualities[1] In future this competition will increase since the Canadian mills are steadily improving both the quality and styles of their manufactures

In the imports of wood, wood products and paper into Canada, the American suppliers have a good hold For instance, of the total imports of this group valued at \$34.2m in 1937-38, the share of U S.A was \$27 8m. and of the U K \$3 9m. The tariff preference has helped the imports from the U K considerably Imports of books and printed matter from the U K are handicapped in competition with those from the U S.A due to geographical contiguity, similarity in reading taste, similarity of trade practice, the higher prices charged for U.K. books, and the practice followed by the British authors of selling Canadian rights to American publishers

Chemicals —The chemicals and allied products are also largely supplied by the U S A But the imports from the

1 Ibid, p 90

U K. have increased under the spur of tariff preference to \$7 7m in 1937-38 Germany is another important supplier Canada has a well organised domestic industry and its output in 1937 was estimated at \$24m Imports of drugs and medicines from the U K rose to \$851,856 in 1937-38 Imports of dyeing and tanning materials amounted to \$694 920 in 1937 38 The U K supplied paints pigments and varnishes worth \$1 8m in 1937-38 It is interesting to note that there is a large paint manufacturing industry in Canada which supplies practically the whole market and imports consist chiefly of articles used for the manufacture of paints The value of domestic output in 1937 was estimated to be over \$24m

British Manufacturers Strengthen Their Hold on the Canadian Market—Thus the British manufacturers have acquired a greater hold over the Canadian market as a result of tariff preferences If the British manufacturers had studied the Canadian market better and shown more adaptability they would have added still more to their exports Further preferences have led to considerable trade diversion and damaged the established trade relations It will also be seen that trade relations are determined by the tastes of the people and the industrial technique and resist therefore the forces working for uneconomic diversion It has to be admitted that tariff preferences cannot help to knit the different parts of the British Empire with their distinct economic requirements not unoften competitive into a single homogenous economic unit Economic limitations of such a plan are obvious It is responsible for tremendous waste of world economic resources

Britain Shares the Domestic Market with the Empire— The increase in trade between the contracting countries has not been one sided The Agreements have also enabled the Dominions and Colonies to capture a port of the British market The following table shows the nature of trade

Imports into United Kingdom from
(in millions)

Year	Canada	Australia	New Zealand	South Africa
1930	38.1	46.4	44.9	20.2
1931	32.8	45.7	37.8	13.1
1932	43.0	46.0	37.0	15.4
1933	46.2	48.6	37.2	14.4
1934	50.4	49.9	40.4	11.9
1935	56.0	54.3	38.1	13.7
1936	75.0	61.4	43.7	13.5

For a proper understanding of the significance of the foregoing statistics it is essential to bear in mind that the imports into Great Britain from the Empire consist largely of raw materials and food grains. The markets for raw materials are much less competitive than those of manufactured goods. In other words, the raw materials and foodstuffs produced within the Empire or elsewhere can find a relatively free market both amongst the units of the Empire as well as in the foreign countries. The case with manufactures is radically different, the markets for manufactured goods are relatively more restricted and competition is increasing. This is particularly true of British manufactures. This important feature must be kept in view while analysing the benefits accruing to the different parties to the agreements.

Another important point to be remembered is the nature of the protectionist policy followed by Britain since the Ottawa Agreements. Britain has been following a most uneconomic protectionist policy, unparalleled in her history. Some of the most inefficient industries are being protected at the cost of the general taxpayer. But it is significant to note that Britain while following a policy of unqualified protectionism at home, has demanded from her Dominions and Colonies that they shall extend protection only to those industries which are reasonably assured of opportunities of success. As a result of this policy of extreme protectionism, the Empire countries have not been able to share the British market adequately. Besides a part of the share they have

obtained in the British market is due to the diversion, under preference, of trade from the non-Empire countries[1]

Diversion of Trade.—The most serious defect of these trade agreements is the artificial diversion of trade they have led to The analysis of Anglo-Canadian trade has shown this[2] Immediately after the negotiation of the agreements this general tendency became conspicuous A detailed analysis of the quality and value of each individual article, after making due allowance for other forces, would show the precise character of diversion Commercial discrimination normally leads to artificial division of trade The working of Ottawa trade agreements has corroborated this statement With the general recovery and improvement in trade this tendency has become a little less conspicuous Further, the adjustments in the structure of industries have partly helped to neutralise the effects of preference The indications are not lacking of preference having exhausted its force in the case of certain articles In the preceding analysis of Canadian imports, general trends in this direction have been noted

At this stage a few more details about the diversion of trade may be noted, by way of illustration In the case of cotton goods the diversion is very conspicuous The imports of British cotton piece-goods into Canada increased from about \$4m in 1932 to \$7m in 1935 36, while the imports from the U S A fell from \$5m to \$2m Similarly, South Africa increased her purchases of British cotton piece-goods and reduced her purchases from foreign countries The imports of woollen piece-goods from U K rose, while those from

foreign countries declined. The trade with Australia, New Zealand, South Africa, etc., shows similar tendencies

In the British markets, likewise, the Empire countries have gained at the cost of foreign countries. For instance the imports of meat other than pig from Empire countries rose from £18m. in 1931 to £20m. in 1935, while those from foreign countries fell from £35.5m. to £22.6m. The imports of Empire bacon and ham increased from £1 7m. in 1931 to £5 8m. in 1935 while the foreign imports fell from £34.6m to £24 6m.

Thus, the Ottawa Agreements have restricted world trade[1] and created fresh complications in modern commercial policy The repercussions of the Agreements have made it abundantly clear to the sponsors that something must be done to remove their defects For instance, the Canadian Agreement in its working showed that Canada's trade with the U.S.A. was being penalised under the discriminatory tariff treatment and that it was in her interest that the situation should be eased. The other Dominions and Colonies have also learnt by experience the economic and political implication of the Scheme Fortunately Canada gave a lead by modifying the agreement

The Anglo-Canadian Trade Agreement of 1937.—The revised Trade Agreement between Canada and the United Kingdom, signed at Ottawa on the 23rd Ferbrary, 1937, marks an important step in the direction of free trade It is distinctly more liberal than the agreement of 1932. A great deal of credit for this measures goes to Mr Mackenzie King The Canadian government have reduced import duties on a long list of British goods, including many important lines of cotton and woollen textiles, chemicals, iron and steel and machinery, etc. The reductions affect about 150 items and sub-items, covering about 40 per cent. of British imports. The United Kingdom has also offered reductions, but their scope is very much restricted. Further,

1 "Thus, the net effect of tariff adjustments made to give effect to the undertakings of Ottawa was more to restrict Empire-foreign trade than to free inter-Imperial trade." Vide Dr Madan, B "India and Imperial Preference" p. 3.

Canada has transferred a large number of important tariff items from the list of those on which a margin of British preference is guaranteed to the list of those on which a maximum rate of preferential duty is guaranteed The United Kingdom, in return, gives merely a pledge to maintain minimum margins between the general and preferential tariffs This puts a serious obstruction in the way of the lowering of trade barriers

The most important feature of the Anglo-Canadian Agreement is not what it contains but what it omits The new pact omits the undertaking Canada had given in the Agreement of 1932 that she would give tariff protection only to those industries which were reasonably assured of sound opportunities of success, and that protective duties would not exceed a level that would give U K producers full opportunity of reasonable competition, on the basis of the relative costs of economical and efficient production, subject to special consideration for infant industries This omission is a sign of most practical and sane economic policy It has already been shown that such a pledge, which is one sided has limited practical utility To this must be added the difficulties of assessing "relative costs of economical and efficient production" The hopes of those who believed that the pledge would check the growth of protectionism in the Dominions were falsified

The new trade agreement has a clause against dumping

Barring these changes the new pact has preserved some of the objectionable features of the agreement of 1932 The changes are largely in matters of detail Except for the minor revision of tariffs and the omission of the undertaking affecting the protection of domestic industries in Canada, the essential features have been scrupulously kept intact For instance discriminatory preferential tariff treatment is continued, and the Empire markets are still double-locked [1] The guarantee of minimum margin of preference is preserved, which limits the scope for reciprocal reduction in

tariffs in commercial treaties with foreign countries and perpetuates discrimination The principle of quantitative restrictions also remains This agreement was further revised in matters of detail in 1938

Let us now state the conclusions which emerge from the preceding survey

1 The Ottawa Trade Agreements have raised rather than reduced tariff barriers on world trade

2 The discriminatory and exclusive tariff treatment has led to uneconomic diversion of world trade Of such a policy economic autarky is the most obvious result

3 The guarantee of a minimum margin of preference has perpetuated discrimination and sealed the scope for reciprocal tariff reductions with foreign countries In fact, it has sealed the possibilities of improvement in international economic relations

4 The adoption of the quota system for regulating imports into Britain has intensified non tariff trade barriers and reduced world trade

5 The most important step in the direction of freer world trade would be for Britain to give the lead by abandoning the policy of Imperial Preference and economic self-sufficiency as embodied in agricultural protectionism

CHAPTER IX

BRITISH COMMERCIAL TREATIES

THAT Great Britain gave up her traditional policy of free trade has been shown in the preceding chapter. Although Britain adopted protectionist policy avowedly as a bargaining weapon for lowering trade barriers in other countries, she has gradually developed it into a system and an essential feature of her trade policy. In this process of transition, the Ottawa Trade Agreements constitute an important link. The agricultural policy formulated for protecting the British farmer, and the trade agreements negotiated since then have strengthened the protectionist system in Great Britain.[1] This definite turn of British commercial policy from free trade to protectionism has been a very powerful force in stimulating the growth of economic nationalism. The future of commercial policy and world trade largely depends upon the lead that advanced countries like Britain and the United States may give. In the following pages an attempt will, therefore, be made to examine the structure of British commercial treaties, other than the Ottawa trade agreements, and their effects on world trade.

Quota Provisions in the Commercial Treaties.—Quotas constitute the most significant feature of the new British commercial policy. Not being satisfied with the aggressive tariff protection, Britain has restored to quota restrictions as a more prompt and effective method of regulating the movements of international trade. The experience of France had made it abundantly clear that quotas could be effectively used for a prompt adjustment of balance of trade. That the economic development during the post-

war period had created new problems for British trade and industries has already been pointed out To meet the new situation, a radical reconstruction in the industrial structure was imperative The reconstruction was, however, not easy to effect To the difficulties created by the vested interests must be added those due to abnormal conditions arising out of the depression and its aftermath Besides the British Government was not prepared to shoulder the responsibilities of this huge task, which might have easily thrown the party attempting it out of power And yet the foreign markets for British goods had to be developed and trade increased With the minimum dislocation to the industrial structure, British trade and industries had to be encouraged under the protectionist system. Tariffs were being gradually raised in order to provide bargaining power Imperial preference had been developed and perfected into a system at Ottawa The commercial treaties negotiated thereafter with foreign countries are based on the principle of bilateral balancing of trade,[1] "buy from those who buy from you" The quotas were found most convenient and effective in achieving this objective

Britain has used quotas for protecting the domestic farmer and encouraging British exports, particularly coal Imports of certain agricultural commodities into Great Britain have been restricted to protect the British farmer The trade agreements contain definite and detailed provisions to that effect

The Ottawa Trade Agreements, as noted in the preceding chapter, contain specific provisions envisaging the contingency of quantitative restrictions of certain imports For a period of three years no quantitative restrictions could be imposed on the imports from the Empire countries of eggs, poultry, butter, cheese and other milk products At the expiration of three years, however, the British

Government was free to impose restrictions in consultation with the Dominion Governments, including quotas, "if necessary in the interest of the U K producers" Thus, it is clear that Britain had already a definite scheme of fostering the growth of British agriculture before it went to Ottawa, and quantitative restrictions were an integral part of this policy The Ottawa agreements merely guaranteed a temporary immunity to Dominion produce in return for substantial and tangible concessions

Thereafter the British Government negotiated trade agreements with a number of countries Some of these agreements contain quota provisions, affecting both imports and exports The quotas regulating foreign imports into Britain may be broadly subdivided into two kinds In some cases, specific minima of imports have been guaranteed, while in others there is a general assurance of most-favoured-nation treatment affecting quota regulations The general structure of quota mechanism has already been examined[1] In the present chapter, therefore, the quota provisions of the British trade agreements will be analysed in detail to find out their effect on world trade

Trade Agreement with Denmark—The Agreement is sufficient The quota provisions are laid down in considerable detail. As regards the agricultural imports the British Government undertook not to regulate the quantity of the imports of bacon ham eggs or cream from Denmark, except in so far as might be necessary to secure the effective operation of a scheme or schemes for the regulation of the marketing of domestic supplies of these products In the event of such regulation of imports being introduced in the case of all or any of these products, the following provisions shall have effect in so far as they might be applicable

In making *allocation* to the several foreign supplying countries, the British Government will take into consideration the position which Denmark has held in recent years

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1 Vide Chapter IV

as a supplier of these products to the British market In particular, for bacon and ham, the Danish allocation will not be less than 62 per cent of the total permitted imports from foreign countries For butter, the Danish allocation will not be less than 2,300,000 cwts in a year If the total imports of butter are allowed to exceed 8,100,000 cwts in any year, Denmark will be allocated her share of the imports in excess of that amount For eggs, the Danish allocation shall not be less than 5½ million great hundreds in any year subject to, however, the undertaking that if some greater reduction in the total imports from all foreign countries than is compatible with this quantity should be essential to secure the maintenance of a remunerative level of prices, the British Government may, after consultation with the Danish Government, reduce the imports of eggs from Denmark below 5½ million great hundreds But the Danish allocation will in no case be less than 38 per cent of the total permitted imports from all foreign countries For cream, any reduction that may be necessary in the quantity of imports from Denmark shall be effected as gradually as possible

In case the total quantity of any of the aforesaid products permitted to be imported into the U K. from foreign countries is increased during the period of regulation, additional allocation will be made to Denmark, but any temporary inability on the part of Denmark to supply the whole or a part of any such additional allocation will not prejudice the undertakings given above as regards any subsequent period In case any other foreign supplying country renounces or forfeits, in whole or in part, its allocation of any of the aforesaid products, the Danish allocation will be increased proportionately

Further, the British Government agreed not to regulate the imports of dried fish or of salmon, sea trout, eels or fresh water fish from Denmark In case imports of other varieties of fish are regulated, they would be subject to following conditions In making *allocations* to the several foreign supplying countries the British Government will

take into consideration the position which Denmark has held during recent years as a supplier of these products to the British market. The total quantity of fresh and wet salted fish permitted to be imported from Denmark will not be less than 412,000 cwts. in any year, exclusive of any salmon, sea trout, eel or fresh water fish. Of the minimum permitted total of 412,000 cwts. not less than 20,000 cwts. will consist of wet salted fish.

Argentine Trade Agreement.—Argentine has been an important supplier of beef to U. K. In the drive to preserve the market for the domestic producer, and commercial bargaining for securing better opportunities in foreign markets for British goods, the imports of Argentine beef into the British market were the subject matter of a trade agreement.[1] The British Government agreed not to impose any restriction on the imports of chilled beef into the U. K. from Argentine in any quarter of the year below the quantity imported in the corresponding quarter of the year ended the 20th June, 1932, except when necessary to secure a remunerative level of prices in the British markets. These restrictions will be removed if it appears that the Argentine imports thus excluded are being replaced by increased imports into the British market of other kinds of meat with the result of neutralising the desired effect on prices. Further, the British Government will not reduce the imports of chilled beef from Argentine to an amount more than 10 per cent. below the quantity imported in the years ended the 30th June, 1932, unless the imports from other countries are also reduced.

Article I of the new Trade Agreement with Argentine,[2] signed on December 1, 1936 provides that in the event of imports of meat from foreign countries being regulated the imports of meat from Argentina will not be less than those specified in the first schedule. Thus, in the case of chilled beef, the minimum quantity to be imported from Argentina in 1937 was that of 1935 less by 138,700 cwts. In each

1. Vide B. T. J., 11-5-1933, pp. 727-29.
2. Vide B. T. J., 10-12-1936.

of the succeeding years 1938 and 1939 the minimum quantity imported was reduced by 138,700 cwts But in 1939 the imports from Argentina were not to be less than 6,590 000 cwts For frozen beef the minimum annual quantity agreed upon is not less than 5 6 per cent. of current imports of chilled beef and frozen beef from Argentina For canned beef and pork, the minimum annual imports from Argentina were fixed at 605 600 cwts and 186 800 cwts. respectively The imports of mutton and lamb not preserved in air tight containers, were to be 886 000 cwts in 1937 and 797 400 cwts. in 1938

Trade Agreement with Norway—The exports of fish from Norway to U K. are important. The Trade Agreement, therefore lays down a definite minimum below which the imports shall not fall. Under the Agreement, the British Government agreed that in the event of quantitative regulation being applied to the imports of fish into the United Kingdom the imports of fish from Norway shall not be restricted so as to be in any one year less than 240 000 cwts. in respect of fresh herrings. The above mentioned quantities are exclusive of any salmon, trout and eel the imports of which will not be subject to quantitative regulation.

Anglo Swedish Trade Agreement.—The Trade Agreement with Sweden contains similar quota provisions In the case of imports of butter and fish definite minima are provided, if imports are subjected to quantitative restrictions. The British Government agreed not to regulate the quantity of the imports into the U K. of Swedish bacon, ham, butter and eggs, except in so far as such regulation may be necessary to secure the effective operation of schemes for the regulation of the marketing of domestic supplies of these or related products In the event of such regulation being introduced the British Government agreed to allot to Sweden "an equitable share of permitted foreign imports,' having regard to the proportion of total foreign imports of those products which has been supplied by Sweden in recent years. Allocation to Sweden will be made on the same basis as in the case of other foreign

countries In regard to butter, the allocation to Sweden will not be less than 185,000 cwts in any year If the total imports of butter into U K are allowed to exceed 8,100,000 cwts in any year, Sweden will be allowed "an equitable share" of the imports in excess of 8,100,000 cwts In case the British Government thought of regulating at any time the imports of fish into the U K, the Swedish imports will not be less than 43,000 cwts, in any year, exclusive of eels and fresh water fish The imports of eels and fresh water fish from Sweden will not be subject to any restriction

From the foregoing illustrations it will be seen that the British Government gives an undertaking not to impose quantitative restrictions, except in so far as it may be necessary to facilitate the marketing of agricultural products in the U K The proviso is sufficiently wide to neutralise the utility of the guarantee clause It is a shrewd move to provide the semblance of free trade, the freedom of action within a fairly wide field remains unfettered The guarantee of a definite quantitative minima violates both the letter and the spirit of the Most-Favoured-Nation-Clause It amounts to discrimination The complications and restrictive effects of such a policy are obvious

In the British trade agreements, as can be seen from the foregoing illustrations, there is an undertaking to allot "an equitable share" in case the imports into Britain are subjected to quantitative restrictions The equitable share is determined on the basis of imports in recent years from the countries concerned For instance, under the trade agreement with Estonia [1] the British Government agreed not to regulate the quantity of imports into the U K of Estonian bacon, hams, butter, or eggs, except for facilitating the marketing of domestic supplies of these or related products In case such regulation is introduced Estonia will be allotted "an equitable share" having regard to her supplies in recent years

This form of quota restriction is more in keeping with the requirements of the Most-Favoured-Nation Clause and provides equality of treatment[1] But so long as the quota regulations are not determined by the reasonable economic requirements of the country imposing them and some countries are guaranteed specific minima, the equality of treatment ceases to exist Under such circumstances, the guarantee of most-favoured-nation treatment provided in the agreements has limited utility

Quotas for British Coal—In return for the quota concessions accorded to foreign imports into the British market, Britain has acquired substantial foreign markets for British coal Several countries have agreed to accord a definite percentage of their market for British coal The following table gives us an idea of the nature of quota concessions secured by British coal in foreign markets

Country	Share of the total market
Denmark	80 per cent
Norway	70 per cent
Sweden	47 per cent
Ireland	77 per cent
Finland	75 per cent
Lithuania	80 per cent
Estonia	85 per cent
Latvia	70 per cent

Under the protocols the British Government has reserved the right to terminate the agreements upon three months notice if in any one year the amount of British coal imported by these countries is less than the share agreed upon The agreements, however, will not be terminated if, during the period between the date when notice of termination is given and the date of its taking effect, quantities of British coal imported by the countries concerned are sufficient to make good the deficiency The specific percentage agreed upon savours of discrimination Besides, the commercial policy based on such agreements is apt to be uncertain in its continuity.

1 Vide, Chapter VI Supra.

Tariff Quotas—Some trade agreements contain tariff quotas[1] For instance, the Government of Finland agreed to permit a fixed contingent of salted herrings at reduced duties on the following conditions

(a) During the first year a total quantity of 1 410 000 kilogrammes at a duty of 50 per cent per kilogramme

(b) For each subsequent year a total quantity of 2 600,000 kilogrammes at a duty of 1 Fmk per kilogramme

(c) Of the quantities allowed entrance at reduced duties, the quantities allotted to United Kingdom will be calcu' ' on the basis of the British share in the total impor salted herrings into Finland for ten years 1923 32

Guarantees against Quota Restrictions—The more va able parts of the quota provisions contained in the tra agreements are those which lay down that in respect ι certain articles the parties will not resort to quantitative restrictions For instance the trade agreement with Argentine Republic[2] provides that no quantitative limitations shall be established on imports into the U K of Argentine articles enumerated in the Second Schedule The articles enumerated are wheat maize linseed, bran and pollards sharp and middlings raw wool unrefined tallow, raw horse hair, sausage casings que branch extract melons, etc Further, in case quantitative restrictions are imposed on articles not enumerated in the First and Second Schedule, Argentine will be accorded most-favoured nation treatment Similar provisions are found in a number of other trade agreements It is needless to add that these guarantees provide invaluable security against sudden and discriminatory changes in the future course of commercial policy Of course, under normal economic conditions these assurances would lose much of their importance, for the obvious reason that quotas, whatever their form restrict world trade and economic prosperity

Thus it will be seen that Britain has achieved only a limited success in the reduction of quotas In this con-

nection the achievements of the reciprocal trade policy of the United States are more outstanding and valuable This is due to the difference in objective guiding the commercial policy in the two countries The American trade agreements programme, based on equality of treatment, has succeeded in its attack on quantitative trade restrictions, though the results would have been much better if other countries had also taken up a more liberal attitude Britain, on the contrary, is using quantitative restrictions for obtaining exclusive advantages in foreign markets A country which tries to stimulate trade by discriminatory advantages helps to raise trade barriers instead of reducing them

Bilateral Trade Balancing—The quota and other instruments of commercial policy have been used for bilateral balancing of trade Great Britain has used the bargaining advantage accruing from her unfavourable balance of trade with foreign countries for stimulating British exports This has meant the displacement of foreign suppliers in these markets by the British goods The goods thus displaced have intensified the competition with British goods in those markets where Britain does not possess the bargaining advantage of unfavourable trade balance The trade agreements contain specific provisions encouraging the bilateral balancing of trade For instance, the Protocol to the Anglo-Latvian Trade Agreement provides as follows

> "The contracting Governments having concluded the Commercial Agreement in the desire to maintain and facilitate still further trade and commerce between the United Kingdom and Latvia, undertake to keep in view the balance of trade between the United Kingdom and Latvia and the Latvian Government having regard to the proportion of Latvian exports finding a market in the United Kingdom recognise that in furtherance of the objects of the Agreement the sales in Latvia of goods the produce or manufacture of the United Kingdom should be increased"

Similar provisions are found in the trade agreements with Finland, Lithuania, Estonia Latvia, etc These provisions have distorted the rtiangular channels of trade

No wonder, therefore, that during recent years multilateral trade has rapidly declined At the same time there has been a marked increase in bilateral trade. This is largely due to trade diversion That distortion of the normal channels of trade has proved uneconomic is too obvious to be dilated upon

Reciprocal Tariff Concessions.—It has been shown that the reciprocal trade agreements programme of the United States has faced the problem of demobilisation of trade barriers Although the progress in the reduction of tariff barriers has not been sufficiently rapid, the programme marks a valuable step in the right direction The sponsors of protectionism in Britain had pleaded that they wanted it for lowering down world trade barriers The Ottawa Trade Agreements raised world trade barriers, instead of lowering them. Now, therefore, we have to ascertain how far other trade agreements negotiated by Britain have contributed towards the demobilisation of trade barriers

The Trade Agreements provide that "The articles enumerated in Schedule to this Agreement produced or manufactured in the United Kingdom from whatever place arriving shall not on importation into be subjected to duties or charges other or higher than those specified in the Schedule" This undertaking contained in most of the trade agreements implies both reduction in duties and stability of tariffs During the tenure of the trade agreement duties on the articles specified in the Schedules attached thereto cannot be raised Further, the scope for the reduction of customs barriers is not in any way limited The tariff concessions are broadly of three types, reduction in duties, consolidation of these reduced duties, and assurance against transfer of articles on free list to dutiable list

An analysis of the Schedules attached to the trade agreements reveals the difference in the nature of tariff concessions accorded in individual cases The tariff concessions offered in indvidual trade agreements have been determined

by the height of tariff barriers raised, the nature of other trade-control measures, the number of articles imported and their quantum, the balance of trade between the countries concerned, their bargaining strength, and the nature of economic policy pursued Naturally the countries which had fairly moderate tariff barriers, could offer relatively less substantial duty reductions as compared with those which had raised their tariffs to excessive and prohibitive heights Similarly, the countries which made frequent and extended use of more effective non-tariff trade control measures, and used customs tariffs sparingly, could not offer any significant tariff reductions In other words, the tariff levels, in view of the emergence of the non-tariff trade control measures, cannot, if taken in isolation, be a true guide of the nature of modern commercial policy For instance, France has used quotas more frequently and extensively than tariffs with the result that tariff level has remained moderate, and the duty reductions are consequently less striking In all such cases tariff reductions have played a relatively moderate role

Valuable tariff reductions have been obtained as a result of the new trade agreements But the duties fixed under the agreements, still, continue to be fairly high Besides, it is difficult to determine how far the reductions are genuine, because frequently tariff-padding has been resorted to as an aid to commercial bargaining Britain is not free from blame in this respect Further, the spirit of economic nationalism is strong and an earnest attempt for reducing trade barriers is lacking Political insecurity and economic imperialism are at the root of the trade barriers Under these circumstances, therefore, the reductions obtained under the trade agreements may be taken to be the best available palliatives

Exchange Provisions.—The circumstances which led to the disintegration of the international monetary mechanism have been already noted. The gaps in the balance of payments of several countries, caused thereby, presented serious problems For the debtor countries the most obvious

solution was either to introduce exchange control or resort to currency depreciation, or a mixture of both. They resorted to exchange control in order to maintain the external purchasing power of their currency. This they could do only by isolating their national cost and price structures from international influences. That exchange control *restricts the flow of international trade* by regulating the means of payment has already been shown in the preceeding section. Exchange control implies differential treatment of imports ignoring entirely the essential economic basis of world trade. The principle of *comparative costs is completely thrown overboard*. That the effective utilisation of world's economic resources has been considerably obstructed by these measures is accepted.

Anglo-Argentine Convention.—The British trade agreements also contain exchange provisions. The Anglo-Argentine Convention signed on *1st May, 1933*, is significant. At the end of 1932 in Argentina the accumulated funds awaiting remittance abroad amounted to about $400 million pesos (paper). The situation became still worse during 1933, when the amount of available exchange fell short of requirements by about $250 m. *All* funds awaiting remittance before 1st May, 1933 (or before 1st February 1933, in the case of imports) were held to be blocked for all countries alike. To obviate the exchange difficulties, thus created, the Anglo Argentine Convention provided *that whenever any system of exchange control is in operation in Argentina*, the full amount of the Sterling exchange arising from the sale of Argentine products in the United Kingdom, after deduction of a reasonable sum annually towards the payment of Argentine's public external debts, *will be available for current remittances from Argentine* to the U K. Further the Argentine Government agreed that out of the sterling exchange thus becoming available, the sterling equivalent of $12m paper pesos will be set aside for payment in cash of claims in respect of peso balances *awaiting on the 1st May, 1933, for remittance to* the United Kingdom. The Argentine Government also

agreed to issue Sterling Bonds in exchange for the peso balances awaiting remittance to the U K. after exhaustion of $12m. paper pesos These bonds will be issued at par, will carry a rate of interest at 4 per cent per annum and will be repayed within 20 years, repayment beginning after five years [1]

The successful working of the convention reduced the incubus of frozen balances and provided the Argentine Treasury liquid funds at a fairly low rate of interest Therefore the Argentine Government offered to issue bonds under similar but slightly less favourable conditions to holders of blocked balances awaiting remittance to other countries The agreements were accordingly entered into which Belgium, Holland, Switzerland, Germany, etc

Thus, the Anglo-Argentine Convention makes it clear that the ability of a country to pay its public or trade debts depends upon the willingness of the creditors or exporting countries to accept its goods in discharge of their claim The problem of blocked balances and frozen claims arose out of the unwillingness of the claimants to accept their payments in goods The blocking of the channels of multilateral trade have created transfer difficulties The exchange provisions of the trade agreements constitute an attempt to minimise the waste of economic resources under present abnormal conditions by bilateral balancing of trade between pairs of countries That this is essentially a compromise can hardly be denied It is an expedient to tide over the difficulties created by the economic and political conditions of the modern world Exchange rationing can never provide a stable basis for world trade

Anglo-Argentine Trade Agreement.—This Agreement signed on December 1, 1936, renews the exchange regulations Article IV provides that whenever any system of exchange control is in operation in Argentina, the Argentine Government will make available, for the purpose of meeting applications for current remittances from

1 Vide B T J., 11 5-1933 p 729

Argentine to the U K, the full amount of sterling exchange arising from the sale of Argentina products in the United Kingdom, after deduction of a reasonable sum annually towards the payment of the service of the Argentine public external debts payable in countries other than United Kingdom[1]

Anglo-Turkish Trade Agreement—The Anglo-Turkish Trade Agreement[2] signed at Angora on June 4, 1935[3] contains very important exchange provisions Article VI *provides that the undermentioned sums due from persons* in Turkey to persons in the U K will be deposited in Turkish pounds on due date in a special account at the Central Bank of Turkey (a) the balances remaining to be paid under the exchange of notes of April, 1935, (b) sums due in respect of British goods imported into Turkey before May 15, 1935, and those imported after May 15 1935, and before this Agreement comes into force, and (c) sums due in respect of British goods exported to Turkey after coming into force of this agreement The sums in Turkish pounds thus deposited will remain blocked in favour of persons in the United Kingdom entitled thereto until they are transferred to the creditors Any difference of exchange beween the day of deposit and the day of transfer will be borne by the debtor

Article VII provides that all sums due from British importers to Turkish merchants in respect of Turkish goods will be payable in sterling on the due date to a bank in the U K specified by the Central Bank of Turkey, and will thereupon be credited to a special non interest bearing account, called, the "Sterling Account," to be opened by the Central Bank of Turkey at that bank The Turkish Government will do their best to secure that any such sums which are paid direct to persons in Turkey will also be credited to the Sterling Account The Turkish Govern-

ment, however, will not be liable for any loss arising out of differences of exchange between the date of payment of any sum and the date it is credited to the Sterling Account Of the sum received in the Sterling Account, 70 per cent will be transferred to a sub-account A and the remaining 30 per cent to a sub-account B The sums referred to in Article VI will be transferred in sterling to the British merchants entitled thereto in the chronological order of their deposit, and within the limits of the sums available in sub-account, A The sums transferred to sub-account B will be at the free disposal of the Central Bank of Turkey

The Anglo-Turkish agreement alos contains provisions for private compensation transactions between the British and Turkish subjects The articles in respect of which private compensation transactions are permitted include carpets, kilems, dried vegetables eggs, fresh fruits, gum, tobacco, vegetable colouring materials and wines and spirits In respect of each one of such transactions the f o b value of the U K goods imported into Turkey will not exceed 70 per cent of the f o b value of the Turkish goods imported into the U K The balance of 30 per cent will be payable by the persons in the U K concerned into the sub-account B, referred to in Article VII of this Agreement Such private compensation transaction will be subject to any quantitative restrictions on imports which are or may be imposed

Anglo-Uruguay Trade Agreement—The trade agreement with Uruguay,[1] signed in 1935, deals with the liquidation of sterling assets "frozen" in Uruguay and the allocations of sterling to meet the U K requirements in the future The United Kingdom funds frozen in Uruguay are to be liquidated by payment of 30 per cent of each claim in cash and by the issue of 3½% five-year sterling bonds in respect of the balance As regards future exchange requirements the Uruguayan Government agreed to make available for United Kingdom requirements each

1 Vide B T J 11 7 1935 p 64.

month a quota of exchange equivalent to at least 76 per cent of the value of the U K imports to Uruguayan products during the last month but one, as recorded in the British trade statistics It is further provided that for each complete period of twelve months the exchange quota must be not less than 80 per cent

From the foregoing analysis it will be seen that exchange provisions were incorporated into some of the trade agreements in order to liquidate frozen claims and provide greater scope for British exports The exchange difficulties experienced by the debtor countries and their inability to ensure prompt repayment of trade and capital debts were in no small measure due to the reluctance on the part of the creditor countries to receive payments in goods The provisions outlined above make it abundantly clear that Britain as a creditor country recognised the necessity of a change in the policy, though late, which had endangered world trade Considerable damage had already been caused to the normal flow of trade by the faulty attitude adopted by the creditor countries The change in policy is, however, based on mere expediency and still ignores the fundamental basis of international trade It amounts merely to a make-shift arrangement for liquidating the past commercial and non-commercial indebtedness and maintaining the flow of trade In the days of narrow economic nationalism the recognition of the principle that international trade is essentially barter augurs well for the future of world trade But another equally important principle that awaits recognition is that international trade is triangular Until the second principle is recognised the flow of trade will be retarded It is essential to note that the undertakings contained in the agreements that the full amount of sterling exchange arising from the sale of goods in Britain, after a reasonable deduction towards the payment of other foreign debts be made available to meet the current British requirements is apt to restrict the flow of world trade in the long run It is evident that Britain has used her bargaining power as a large scale purchaser of Argentine products, to ensure a direct payment of trade and

capital debts to her There is thus a definite swing from a triangular to bilateral balancing of trade Under the new arrangement, therefore, other countries are apt to be adversely affected, for Argentine will have to restrict her purchases from other countries The United States of America, in particular, will feel the adverse effects of the discriminatory treatment accorded under this agreement Of course, Great Britain is not alone to blame for distorting the channels of trade, other countries have their share Britain, France and the U S A could have, however, given, in time, proper lead in the direction of freer world trade

Besides, such an arrangement is not in keeping with the spirit of the Most-Favoured-Nation Clause, it savours of discrimination The ear-marking of the full amount of sterling exchange for meeting British claims amounts to discrimination in favour of British claimants Accepting the triangular basis of world trade, the most-favoured-nation policy requires that the British creditors, commercial or non-commercial, must rank on the same footing as those from other countries No preference or discrimination may be shown. The Most-Favoured-Nation Clause, therefore, is shorn of its significance by these exclusive and discriminatory arrangements which have complicated international economic relations For instance, under the Anglo-Argentine Commercial Convention "the Argentine Government undertake that in no event shall applications for exchange for remittances to the United Kingdom, whether in respect of peso balances or of current transactions, be less favourably treated than similar applications for exchange for remittances to any other country" This is an undertaking for according equality of treatment in respect of claims of exchanges But the pledge loses its importance when we recall the clause which provides that the full amount of sterling exchange shall be made available exclusively for meeting the British claims Britain ought to have adopted the policy of equality of treatment in the allocation of exchanges

It is significant to note that in some trade agreements Britain has got an undertaking from foreign countries not to impose any tax on foreign exchanges required to pay for British goods and services For instance, under the Anglo-Latvian Trade Agreement the Latvian Government declare that they have no intention of imposing a tax on purchases of foreign exchange required for the purposes of *payments in respect of goods imported into* Latvia *from* the United Kingdom or of payments due to United Kingdom shipping interests The British Government has reserved the right of terminating the agreement at three months' notice if any such tax is imposed This clause is a distinct and valuable contribution towards the reduction of trade barriers

Most-Favoured-Nation Clause.—The British attitude towards the Most-Favoured-Nation Clause has recorded a marked change during the recent years That Britain has imposed substantial tariffs on a wide range of commodities and formulated an extensive system of Imperial Preference at Ottawa has been shown Though technically recognised as exceptions, the network of preferences amounts to *de facto* discrimination and is greatly responsible for the present wave of economic insanity Similarly, fairly high import duties imposed on an extensive list of British imports have given a remarkable spur to higher tariff levels in other countries In this race of trade barriers, the most-favoured-nation policy has received a serious setback No wonder, therefore, that other countries are not prepared to accord unconditional most-favoured-nation treatment to protectionist Britain, reciprocity has become the rule

Britain has, accordingly, modified its attitude towards the unconditional Most-Favoured-Nation Clause Explaining the British policy, Mr Runciman has said "Countries entitled under existing treaties to most-favoured-nation treatment will enjoy the benefits of any reductions which are accorded by the arrangements now being negotiated *with other foreign countries, and they will certainly not*

be prepared to continue indefinitely to accord full most-favoured nation treatment to countries which show themselves unwilling to meet the reasonable requirements of this country, in regard to the treatment of United Kingdom goods" Thus, British policy in negotiating commercial treaties since 1933, has been to accord most-favoured-nation treatment on the basis of reciprocity The British Government has approached individual countries for reciprocal concessions, instead of introducing the M F N Clause in a revised form in commercial treaties The commercial relations with each country have been studied and discussed independently The modification or abandonment of the unconditional Most-Favoured-Nation Clause is to be attempted as a last resort, after all commercial negotiations have failed The form of the Clause is to be determined after consultation with the foreign country concerned This device has enabled Britain to escape the difficulties incidental to general revision and at the same time acquire substantial reciprocal concessions from foreign countries It has been used as an effective bargaining weapon

It is interesting to analyse the structure of the trade agreements from this standpoint The Anglo-Lithuanian Trade Agreement provides for the most-favoured nation treatment in the following terms [1]

'During the currency of this Agreement United Kingdom goods in Lithuania and Lithuanian goods in the United Kingdom shall enjoy in all respects treatment not less favourable than that enjoyed by goods produced or manufactured in any other foreign country"

This unconditional reciprocal and unlimited Most-Favoured-Nation Clause is not found in all trade agreements It is essential to note, however, that the efficacy of the Most-Favoured-Nation Clause is neutralised by the presence of *quota* provisions laying down definite minima. These definite minima, either in respect of commodities or foreign exchange, are essentially discriminatory and destroy

the very basis of equality of treatment Under such circumstances, the Most-Favoured-Nation Clause loses its significance

The Anglo-French Commercial Agreement provides for unconditional reciprocal limited most-favoured-nation treatment in the following terms [1]

"The minimum tariff shall be applied upon importation into the customs territory of France to all goods (with the exception of the articles enumerated in Schedule A' annexed to this Agreement) which are the produce or manufacture of the United Kingdom and are also consigned therefrom, and goods, which are the produce or manufacture of the customs territory of France and are also consigned therefrom (with the exception of articles enumerated in Schedule 'B' annexed to this Agreement) shall be subject upon importation into the United Kingdom to the lowest duties to which like goods being the produce or manufacture of any other country and consigned therefrom are subject"

Here it is interesting to note that the most-favoured-nation treatment is limited to tariffs, and in addition, certain articles are excepted therefrom The Lithuanian agreement, on the contrary provides most-favoured-nation treatment "in all respects" This limitation on the most-favoured-nation treatment undermines the equality of treatment, for non-tariff trade control measures are left entirely unregulated under this form of the Clause For providing an effective equality of treatment it is essential that all forms of trade controls must be brought within the ambit of the Most-Favoured-Nation Clause The unconditional reciprocal and unlimited form of the Most-Favoured Nation Clause incorporated in commercial treaties and enforced in right spirit, would effectively secure equality of treatment

Further, there are a number of trade agreements in which the Most-Favoured-Nation Clause is not specifically provided The trade agreements with Denmark, Argentina, Norway Sweden, Ireland, Latvia Estonia, Finland, etc, do not contain the Most-Favoured-Nation Clause In the

absence of Most-Favoured-Nation Clause, these trade agreements amount to a mere barter of certain reciprocal concessions The British Government probably thought it expedient to exclude the Clause from the trade agreements since it would fetter their discretion in bargaining for discriminatory concessions Thus, under the new trade agreements discrimination is encouraged and equality of treatment has become a distant dream.

Administrative Protectionism—The use of administrative protectionism for regulating imports has increased considerably since the Great Depression, it has become an integral part of the technique of modern commercial policy The most-favoured-nation obligations have been conveniently evaded and differential treatment is accorded to goods according to the country of origin It is obvious, therefore, that a trade agreement which attempts to provide for equality of treatment must include definite provisions regulating the use of administrative control

British trade agreements contain a number of important provisions directed against this form of protectionism The possibility of concessions being nullified or impaired through administrative protectionism or otherwise by the contracting parties has been very scrupulously guarded against For instance, the Anglo-Latvian trade agreement provides as follows —[1]

> The Latvian Government will not operate any restrictions which may he in force in a manner which would have the effect of preventing the benefits of the tariff concessions specified in the First Schedule from accruing to goods the produce or manufacture of the United Kingdom or of the territories referred to in paragraph 2 of Article I, respectively

> The Government of the United Kingdom will not impo e quantitative restrictions on imports into the United Kingdom which would have the effect of preventing the benefits of the tariff concessions specified in the Second Schedule from accruing to goods the produce or manufacture of Latvia provided that this Article shall not apply to such restrictions of imports as may be necessary to secure the effective operation of a

scheme or schemes for the regulation of the marketing in the United Kingdom of agricultural products

The scope of this clause is fairly wide and provides adequate protection against different forms of administrative protectionism Similar provision is, therefore, found in most of the trade agreements

Further, in respect of the enforcement of quota regulations, the trade agreements provide that allocations "will be made on the same basis as, and on conditions not less favourable than, allocations to any other foreign country" To this must be added the pledge that before compulsory quantitative regulations are enforced the Government of the country affected thereby will be given "an opportunity of discussing the allocation" These provisions provide a valuable safeguard against discriminatory restrictions

The trade agreement with Norway provides for mutual national treatment in respect of internal duties Article 3 lays down that internal duties in the U K on the Norwegian goods will not be greater than the duties levied on the similar goods produced in Norway In no case shall such duties be more burdensome than the duties levied in similar circumstances on the like goods of any other foreign country [1]

The trade agreement with Finland makes detailed provisions for regulating administrative protectionism Part IV of the protocol to the Agreement lays down conditions to which the imports of British whisky and gin into Finland may be subject The duties to be levied will be the same as those levied on brandy or rum No discrimination will be made in Finland between British whisky and gin and native spirits in respect of the levy of internal taxes on the sale, transport or consumption of these products The U K spirits shall be accorded most-favoured-nation treatment in Finland The purchase, sale and distribution of wines and spirits will be entrusted exclusively to the Finnish monopoly The British merchants, however, will be given facilities for all legal forms of publicity [2]

The trade agreements provide that any dispute that may arise between the parties as to the proper interpretation or application of any of the provisions will be referred to the Permanent Court of International Justice unless the parties agree to settle their dispute by some other agency or method. The decision will be given in accordance with summary procedure This provision secures prompt and impartial judicial settlement of disputes, and imparts thereby invaluable stability to commercial relations between nations The free play of individual caprice and discrimination is checked. The utility of this provision in these days of economic nationalism is too obvious to need any special emphasis

Miscellaneous Provisions

Agreements Entered into by Commercial Bodies.—In some cases the agreements entered into by commercial bodies are made an integral part of commercial treaties. The Protocol to the Anglo-Danish Trade Agreement takes note of three agreements concluded between the Danish and British commercial bodies. The Protocol to the Anglo-Swedish Trade Agreement takes note of the arrangements between the British coal exporters and the Swedish buyers and users of coal. The right of the British Government to terminate the agreement is made conditional upon the assurance given by the British coal exporters with regard to prices, qualities, availability of the supplies etc., being implemented. The Anglo-Irish Trade Agreement takes note of similar arrangement between the commercial interests in the two countries affecting the sales of British coal. The Protocol to the Anglo-Finnish Trade Agreement takes note of the arrangements between the British and Finnish merchants affecting the sale of wheat flour iron and steel, commercial motor vehicles, jute, cloth, salt and the products of Finnish wood working industries. Similar provisions are contained in the trade agreements with Lithuania, Estonia, Latvia, etc.

Official recognition of the arrangements agreed to between commercial interests in the contracting countries

is a very useful feature Within a certain ambit, private initiative in commercial negotiation is apt to yield prompt and more tangible results, better suited to the requirements of the parties concerned Besides, it makes the task of the state representatives negotiating a trade agreement easier This sort of arrangement will inspire better confidence in the business community The critics of modern commercial policy will be well-informed and responsible It is essential that the public should be taken into confidence in moulding commercial policy

Encouragement to British Shipping—Some of the trade agreements contain definite provisions for the increased utilisation of British shipping For instance, the Anglo-Lithuanian Trade Agreement provides that the Lithuanian Government will promote by all means at its disposal the increased utilisation of British shipping services in the Anglo-Lithuanian trade, and will take no action which would affect prejudicially any British shipping company now engaged in the trade between the two countries, so long as the company maintains existing freight rates and services In case the company makes any substantial changes in the freight rates charged or the services offered, the Lithuanian Government will before taking action, consult the British Government Similar, provisions are to be found in the trade agreements with Estonia, Latvia, etc These provisions give invaluable assistance to British shipping in these days of growing economic self-sufficiency At the same time, efficiency and economy of shipping facilities are adequately safeguarded so that the users of transport services have no cause to complain

There is a saving clause in some of the trade agreements which provides that the rights and the obligations arising out of the previous treaties are not affected by the present agreement

Duration of the Trade Agreements.—As regards the duration of the trade agreements, in most cases the tenure is three years or less The agreements may be continued beyond the specified period if not terminated by the parties

In view of the rapid and marked changes during recent years in the technique of modern commercial policy, the tenure of three years imparts stability and certainty to commercial practice, though it would certainly be much better to extend the period to five or even seven years. But it is essential to note that there are a number of provisions, as has been shown in the preceding discussion, which may be utilised to terminate the agreements before even the expiration of the initial period Thus, the tenure of the agreement depends essntially upon the attitude of the contracting parties, and their earnestness to follow a relatively smooth and stable commercial policy Notwithstanding the relatively short initial period of three years, the *de facto* tenure of the agreements can be extended indefinitely according to the requirements of the parties Given an earnest desire for mutual understanding and accommodation, the initial tenure, though short, will not present any serious difficulties in the continuity of the agreements

Commercial Bargaining.—From the foregoing analysis of the structure of bilateral trade agreements it will be seen that Great Britain has extracted the utmost from the other countries with the aid of her bargaining power The tariffs of 1931 and 1932 and the power of quantitative regulation of certain agricultural imports equipped the British Government with a new and powerful weapon for bargaining commercial concessions from the Empire as well as foreign countries That Britain has made an effective use of this new weapon can hardly be gainsaid The concessions extracted from the Empire countries at Ottawa in 1932 have been analysed in the preceding chapter The structure of the agreements negotiated thereafter with foreign countries analysed in the foregoing pages shows the skill and ingenuity used by the British negotiators in extracting maximum commercial advantages from the other contracting party, irrespective of their effects upon third parties or the world trade The extraction of immediate advantages has been the sole guide of the commercial treaty policy, to the

utter disregard of the general effects on the movements of world trade

That the agreements are based on the narrow and hard commercial bargaining, which sealed the fate of the World Economic Conference and clouded the future of world trade will now be shown Britain has concluded a number of bilateral trade agreements with foreign countries—notably with the Scandinavian countries Argentina, Poland, the Soviet Union, the three Baltic States, and the United States Taking the Scandinavian countries we find that the United Kingdom had an adverse balance of trade with these countries In 1930, the imports from the U K into Scandinavia were valued at 787 million Kroner and exports to the U K at 1 517m Thus, Britain had an adverse balance of trade The other more important countries trading with Scandinavia are Germany and the U S A In 1930 imports from Germany were 1 354m and exports to Germany 568m Germany's balancing of trade was favourable From the U S A imports were valued at 526m and exports 226m during the same period America, too, had a favourable balance of trade Under these circumstances Britain resorted to tariff bargaining and bilateral balancing of trade in order to increase her exports to Scandinavia Her adverse balance of trade strengthened her bargaining capacity Britain, therefore, expected to double her exports at the cost of Germany and the U S A

Anglo-Danish Trade—Let us analyse in greater detail some of the chief imports of the three Scandinavian countries Here again the statistics of 1930 may be studied In the case of Denmark imports from the United Kingdom amounted to about one-seventh of the total imports There is a part of the Danish market, consisting of oilseeds, coffee tobacco petrol etc, for which the U K does not compete This share has been estimated to be about Kr 400m Excluding this share the total market where British goods compete is about Kr 1,300m The more important articles are coal vehicles, and machinery, pig iron, manufactured iron goods, apparel and footwear, woollen

goods, cotton manufactures, etc Of the total imports in 1930, about 55 per cent were supplied by the U K, and 25 per cent by Germany Of the imports of vehicles the share supplied by the U K., Germany and the U S A were 11, 48 and 28 per cent respectively In all other articles Germany has a dominant hold over the Danish market

As regards the Danish exports British market is invaluable Denmark depends primarily upon the British market for her exports This is particularly true of bacon butter, eggs, fish, etc In 1930 total Danish exports of bacon were valued at Kr 510m The whole of Danish bacon was exported to the U K Of the total Danish exports of butter, valued at Kr 437m in 1930 296m worth were exported to the U K Similarly the total exports of eggs in shell from Denmark were valued at Kr 82m. in 1930, of which Kr 70m were taken up by the U K About 50 per cent of fresh fish exported from Denmark was taken by the U K The German prohibitions on the import of dairy produce since 1930 have increased this dependence of Denmark on the British market

The British Government has exploited to the full the economic situation depicted above, of which the Anglo-Danish Trade Agreement is an eloquent testimony Under the Agreement Denmark is guaranteed 62 per cent of the total permitted imports of bacon and hams into the U K from foreign countries The British Government, however, reserve the right to regulate bacon imports "to secure the effective operation of a scheme or schemes for the regulation of the marketing of domestic supplies of these products" In 1930, Denmark supplied 67 per cent of the total British bacon market Under the agreement, Denmark is permitted only 62 per cent of the total permitted imports from foreign countries Further, taking into account the pledges given under the Ottawa Agreements and the Pig Reorganisation Scheme, the guarantee of 62% is meagre, indefinite and illusive Again, Denmark is guaranteed an annual quota of not less than 2 300 000 cwts of butter, with a proviso for a *pro rata* increase if the total

imports of butter into Britain from foreign countries are larger than 8,100,000 cwts This quota accords Denmark a much smaller share of the British market than enjoyed by her before the negotiation of the Agreement The case with eggs is similar In respect of eggs, Denmark is accorded an annual quota of not less than 5,500,000 great hundreds, subject to the proviso that the British Government many, "after consultation with the Danish Government, subject the import of eggs from Denmark to such reduction below 5½m great hundreds as may be necessary to secure the maintenance of a remunerative level of prices in which case Denmark is to obtain not less than 38 per cent of the total permitted foreign imports of eggs into Britain" Before the agreement the Danish exports of eggs to the U K were 8,392,000 great hundreds To this must be added the schemes for encouraging the domestic industry which would substantially reduce the market for foreign suppliers Thus, the concessions accorded by Britain are restricted and relatively indefinite

In return for the aforesaid concessions, Denmark agrees to take at least 80 per cent of her annual total coal imports from the U K This quota is significant when we recall that in 1930 Britain supplied only about 55 per cent of the Danish market, the rest being shared by Germany, Poland, etc Thus under the Agreement, the U K has acquired a valuable concession which would immediately increase the hold of British coal on the Danish market, largely at the cost of Germany and Poland It would lead to diversion of trade Further, the Agreement takes note of private negotiations which aim at increasing British exports to Denmark of iron and steel and maintaining the use of British salt, saltpetre, wrappers, and paper for Danish bacon and ham So also, on a large number of British articles Danish import duties are lowered and stabilised This is a welcome feature of the agreement A clause also provides that in the event of a substantial increase in Danish imports of certain goods from countries other than Britain, measures shall be discussed between

the two Governments "for the purpose of preserving or restoring economic level of prices."

Thus, in return for a few qualified and indefinite assurances that the prospective quota system will not be operated in such a way as to restrict unduly British imports of Danish farm produce Denmark has been led to resort to the regulation of her imports of coal and to accord to Britain a discriminatory quota of 80 per cent It would not be an exaggeration to say that the British commercial policy has stimulated the growth of the quota system. So also, discriminatory practices have led to retaliation The discriminatory quota for British coal extracted from Denmark led to retaliation against Danish exports by both Germany and Poland.

The Danish interests have not profited from the trade agreement The exports of Danish goods to the U K. have declined from Kr 815m. in 1931 to Kr 744m. in 1936 The agricultural exports have not fared better The exports of bacon have recorded a steep decline from Kr 510m. in 1930 to Kr 345m. in 1936 The Danish exports of butter to the U K. have fallen from 123,300 tons in 1931 to 109,742 tons in 1936 The exports of eggs have slightly improved from about 7m. in 1931 to 8m in 1936 Thus Denmark has not derived any material advantage from the trade agreement On the contrary, her exports have received a definite setback.

The United Kingdom has, on the other hand, reaped substantial benefits. The total imports of British goods into Denmark have increased from Kr 219m. in 1931 to Kr 542m. in 1936 Analysing the figures in detail we find that the imports of British coal rose from Kr 27 5m. in 1931 to Kr 69m. in 1936 The imports of British coke rose from Kr 19m. in 1931 to Kr 37m. in 1936 The Polish coal has suffered a serious setback in the Danish market German coal has also lost some ground. Thus, Britain has increased her hold over the Danish market largely at the cost of Poland.

The Anglo-Danish agreement provides for the purchase of British salt corresponding to the quantity used by the Danish slaughter houses and dairies in the manufacture of bacon, ham and butter to be exported to the U K The consumption of British salt for these purposes in the Danish market has increased from about Kr 1m in 1931 to Mr 1 6m in 1936 In other articles of export also Britain has made a substantial improvement in the Danish market

British Trade with Norway and Sweden.—The concessions derived by Britain under the trade agreements with Norway and Sweden are much less striking Norway and Sweden have been able to bargain much better than Denmark because their dependence on the British market is not very great Norwegian and Swedish exports are well distributed Nevertheless, the British market is very important for both the countries Germany, the U S A, Russia, France, Holland, Denmark etc are other more important customers of Norway and Sweden Of the two Sweden finds Great Britain by far the best customer, as she purchases about a quarter of her total exports The most important articles purchased are paper, pulp and timber But it is essential to note that America is also an important purchaser of Swedish paper and pulp and timber finds a ready market in France and Netherlands as well Germany is the chief market for her iron ore Thus, it will be seen that, though Britain is an important customer, Sweden's dependence over the British market is not so great as that of Denmark

Looking to the import trade we find that British ships, vehicles and machinery find a ready market in Norway The position of the U K is very strong In the mineral market also British goods have a very favourable position But the imports of British textile goods are relatively small as compared with those from Germany Thus, Norway offers a very valuable market for British textile goods Britain holds a similar position in the Swedish market In coal and cotton yarn and tissues Britain leads, but in the

case of chemicals, machinery, woollen tissues, hosiery and clothing, both Germany and the U S A have proved successful competitors of Britain

In view of the aforesaid facts the terms of the trade agreements with Norway and Sweden are different from those of the Anglo-Danish Trade Agreement There are a few reductions in import duties and a limited assurance against further increases The Norwegian tariff schedule contains 57 tariff items of which 33 cases are of stabilisation, while the Swedish Schedule contains 104 items, stabilising the *status quo* in 70 cases In the remaining cases there are slight reductions in the already relatively moderate Scandinavian tariff

The tariff concessions conceded on the British side are of greater importance The British Government undertakes, *inter alia* that iron ore, telegraph poles, wood pulp, newsprint, etc, shall remain on the free list The duty on certain classes of soft wood, box boards and granite blocks is reduced from 15 per cent to 10 per cent The duty on craft and various classes of wrapping papers is lowered from 25 per cent to 16-2/3 per cent and that on certain classes of writing paper from 20 per cent to 16-2/3 per cent In addition, the duty of 33-1/3 per cent on steel imports is reduced in the case of certain high-grade steels to 25 per cent and 20 per cent *ad valorem*, according to the price range, but with the proviso that a specific duty may be charged which will have the effect of increasing the *ad valorem* duty in the event of any lowering of existing prices Finally, the existing 10 per cent tariff is stabilised on a large variety of articles including fish, butter and eggs in which Scandinavia is interested In addition, there are quota concessions

An analysis of the statistics of trade may now be made The imports from Britain into Norway have risen from Kr 152m in 1933 to Kr 318m in 1937 The imports of British coal have increased from 883,691 tons in 1932 to 1,661400 tons in 1937 It is interesting to note that during this period imports of coal from Poland have declined from

896,261 tons to 388,671 tons Thus, British coal has strengthened its hold over the Norwegian market at the cost of Poland In respect of other articles as well, Britain has almost doubled her exports to Norway The Norwegian exports to the U K have increased from Kr 114m in 1933 to Kr 236m in 1937

The study of Anglo-Swedish trade under the trade agreement is equally interesting The Swedish exports to the U K have risen from Kr 285m in 1933 to Kr 371m in 1936 During the same period imports of British goods into Sweden have risen from Kr 197m to Kr 308m Thus, both the countries have gained from the agreement, but of the two Britain has had a better share It may be noted that imports of British coal into Sweden have exceeded the quota assigned to the U K under the Agreement

Anglo-German Trade Agreement—This agreement is more restricted in scope than the Scandinavian agreements analysed above Germany agrees to issue licenses for importation into German customs area of British coal and coke up to a maximum of 180 000 metric tons and undertakes "that in the event of German consumption of coal exceeding an equivalent of 7,500 tons of coal in any month there shall be a proportionate increase in the imports licensed from Britain" In return, Britain undertakes to make a reduction of about 5% in her import duties on a few articles like musical instruments, clocks, jewellery, safety razor blades, etc, leaving the general level of duties at 15 to 25 per cent

Apart from the baneful effects of the import quotas, it is essential to note that an increase of 80 000 tons a month in the exports of British coal, guaranteed under the agreement, would not enable her to export 5½m tons which she did in 1929 Again, the British tariff level ranging from 20 to 25 per cent is unwarranted bv her reasonable economic requirements and must strengthen the case for restrictive measures taken by smaller states in self-defence

Anglo-Argentine Trade Agreement—This Agreement originally signed in 1933 and renewed with slight

modification in 1936, is of a different type It deals with exchange difficulties as well as other forms of trade restrictions Exchange provisions have already been analysed in the preceding section Argentina depends upon the British market for the exports of her agricultural products, especially chilled and frozen beef Britain, therefore, agreed not to restrict imports of Argentine chilled beef below the level required under the Ottawa Agreements except in so far as such restrictions might become necessary in order to secure a remunerative level of prices in the British market Such restrictions will not be maintained if it appears that meat from Argentina is being replaced by increased imports of meat from other countries, neutralising thereby the desired effect on prices The imports were not to be reduced by more than 10 per cent without consulting all the chief meat-exporting countries including those in the British Commonwealth Any further reduction, if agreed upon, would be shared by the Dominions Similarly, frozen beef, mutton and lamb were not to be restricted below the Ottawa level without a similar sacrifice by the Dominions

These provisions, have been modified to a certain extent under the new Agreement The Argentine Government has agreed to the imports of foreign meat into Britain being taxed, but the import duty shall not exceed ¾d per lb on chilled beef, 2/3d per lb on frozen beef and 20 per cent *ad valorem* on other varieties of meat No duties will be imposed on mutton, lamb and pork. Further, the imports of chilled beef from Argentina will not be reduced from the 1935 level by more than 2 per cent in 1937, 4 per cent in 1938 and 5 per cent in 1939 Imports of other varieties of meat are subject to similar conditions In addition, Britain has agreed not to increase the duty on wheat or impose any quota restrictions thereon Similarly, the imports of maize will not be subject to any restrictions either in the form of import duty or quota regulations In return Argentine Government has agreed to admit coal and coke free of duty and to reduce import duties on

textiles machinery and vehicles pottery chemicals food and beverages sports requisites etc

Anglo Argentine Trade—The statistics of Anglo Argentine trade show that Britain has derived substantial advantage from the bargain British exports to Argentina have risen from £10 7m in 1932 to £20 1m in 1937 while the exports from Argentina to U K during the same period increased from £48 7m to £59 9m It may however be noted that Argentine exports to the U K had tended to decline until 1936 and it is in 1937 that we note a sudden increase of 33 per cent over the figure of the previous year The Argentine maize has profited most exports to the U K having risen to £18 7 in 1937 Exports of wheat have risen to £7 2m in 1937

Anglo Polish Trade Agreement—Under this Agreement substantial concessions are accorded Poland has agreed to reduce import duties on about 340 British articles including herrings chemicals textile goods machinery motor vehicles and accessories etc On about 110 articles Polish import duties are consolidated In return Britain has agreed to maintain the existing tariff treatment on a number of Polish exports Further Britain has promised that in case imports of agricultural produce are regulated Poland would be allowed to send not less than 41 4 per cent of the quantity of bacon she sold to Britain in 1932 and not less than 13_{2} per cent of the total permitted imports of eggs from foreign countries

The Anglo Polish Trade Agreement has given an invaluable spur to British exports The total volume of imports from the U K into Poland rose from 86m zlote in 1934 to 149m. zlote in 1937 while during the same period exports from Poland to the U K rose from 192 zl to 219 zl only It may also be noted that the rise in Polish exports to Britain has been at a much slower rate as compared with the total trade of the country Poland had to find outlets for her goods in other markets through trade agreements

Anglo Soviet Trade Agreement of 1934—This Agreement is significant in that the ratio between the Russian

exports to imports from the U K is definitely fixed Prior to the agreement Russia had enjoyed a highly favourable balance of trade with the U K The agreement provides that the U S S R, "being desirous of applying in an increasing proportion the proceeds of the sale in the U K of goods imported from the U S S.R to payments for goods purchased in the United Kingdom and for the utilisation of British Shipping Services," agrees to make payments in Britain in each year bearing the following ratios to the proceeds of the U S S R trade with the United Kingdom.

1934	1	1 7
1935	1	1 5
1936	1	1 4
1937	1	1 2
Thereafter	1	1 1

The Schedule attached to the agreement outlines in detail the method of calculating the balance, and makes allowance for payments for the use of British shipping for the repayment of credit, and for all goods bought in the U K

Another important feature of this agreement is the provision of the Most-Favoured-Nation Clause It may be recalled that the Ottawa Trade Agreement with Canada contains a clause to the effect that if either Government is satisfied that preference granted by the Agreement in respect of any particular class of commodities is likely to be frustrated by the creation or maintenance of prices through state action on the part of any foreign country, that Government will prohibit the importation of such commodities from the foreign countries concerned for such time as may be necessary to ensure the effectiveness of preferences This provision was primarily intended to protect Canadian trade against unfair Russian competition The Canadian Government was afraid that, the Soviet trade being a state monopoly, the prices of certain Russian articles in the competitive markets might be reduced to uneconomic levels, particularly in the case of timber and wheat This led to the cancellation of the Anglo-Soviet treaty of 1930, which provided for the most-favoured-nation

treatment The present agreement, therefore, provides mutual most-favoured-nation treatment, but if the prices of any particular imported commodity are likely to frustrate preferences accorded or adversely affect the production of goods, the aggrieved party, if no satisfactory settlement is reached, can except the imports complained of from most-favoured-nation treatment Thus, derogation from the most-favoured-nation treatment is permitted under certain circumstances in respect of particular commodities

Further, the agreement provides that British exports to Russia will be included without discrimination under guaranteed credit scheme In view of this clause, substantial credit has been made available to Russia, with the collaboration of the Export Credits Guarantee Department, for expenditure on British manufactures The Anglo-Russian trade under the Agreement has increased substantially

Anglo-Iceland Trade Agreement.—This Agreement follows the same technique of commercial policy The Government of Iceland has agreed to reduce import duties on some articles and to stabilise its tariff on a few others Further, British coal has been accorded a quota of not less than 77 per cent of the total Iceland imports of coal In return, the British Government has agreed that duty on salted fish imported from Iceland will not be more than 10 percent *ad valorem*, that under a system of quantitative import regulation Iceland's quota will not be less than 354,000 cwts of fresh and wet salted fish, that imports of frozen mutton and lamb from Iceland will not be subject to more severe restrictions than those from any other foreign country

Anglo-Finnish Trade Agreement.—Finland, under the trade agreement, has reduced duties on most classes of cotton textiles, wool and silk mixtures, jute and linen, herrings, tinplate, motor cars and spirits, while the duties on cotton and wool yarns types and linoleum are stabilised Further, Finland has agreed to import from Britain not less

than 75 per cent of her total imports of coal To this must be added purchase agreements On the British side duties have been reduced and consolidated The most important departures are that the duty on birchwood is consolidated at 10 per cent and the duty on the wooden sewing thread reels is reduced from 20 to 15 per cent

The Anglo-Finnish Trade has increased since the negotiation of this agreement Exports from the U K to Finland increased from 435m Marks in 1931 to 1,090m in 1934 and the Finnish imports into the U K rose from 1,991m to 2,913m during the same period Finland has a large favourable balance of trade

Anglo-French Trade Agreement.—The most important contribution made by this Agreement is that it put an end to the tariff war The French Government agreed to apply minimum tariffs on the import of British goods, subject to certain exceptions In the case of British industrial products and coal, French quotas were stabilised and equitable treatment was guaranteed in other respects In return, the British Government agreed to apply lowest tariffs on French goods subject to certain exceptions Further, the British Government agreed to remove the discriminatory surtax of 20 per cent imposed on certain French goods, and not to increase the import duty on French brandy or the aggregate duties (basic duty and surcharge) applicable to French sparkling wines Import duties on French silks were revised and the duties on certain other articles were consolidated

Trade Agreements with the Baltic States.—These agreements have brought valuable concessions for British goods. Lithuania reduced or stabilised the import duties on a number of articles including sauces salt, herrings, cement, glass plates for photography, coal coke, types and tubes, sheets of iron and steel, tin, gramophones, motor cycles, motor cars, chassis for commercial vehicles, cotton yarn, woollen yarn, etc British coal was accorded a quota of 80 per cent In return the British Government agreed to reduce or stabilise duties on Lithuanian goods including

butter, bacon and hams, eggs, wood pulp, ply wood etc Further, the British Government agreed to accord most-favoured-nation treatment to Lithuanian butter, bacon, and ham in case imports of these products into Britain are regulated under quota basis

British exports to Lithuania have recorded a rapid rise from Lits 18m in 1931 to Lits 35m in 1934 Lithuanian exports, on the contrary, have shown a trend towards decline, the value having fallen from Lits 78m in 1932 to Lits 63m in 1934 The exports of Lithuanian bacon have received a setback due to the introduction of import restrictions by Britain

The Government of Latvia, under the Anglo-Latvian Trade Agreement, reduced import duties on a large number of articles including mustard sauces, whisky, gin, rum, salted herrings, coal, coke, tyres, glycerine, tin, tinplates, sewing machines, safety razor blades, gramophones, motor cycles, motor cars, chassis, carbon paper, cotton yarn, wool yarn, etc Britain was also guaranteed a large quota for salted herrings Further, the Latvian Government agreed to purchase 70 per cent of her total imports of coal from Britain In return the British Government agreed to reduce and stabilise duties on Latvian goods, including butter, bacon and ham, eggs, canned herrings, bilberries, cranberries, flax, newsprint, wood pulp, wood match splints, tissue paper, paper, kraft paper, gypsum, tea, etc Further, the British Government guaranteed most-favoured-nation treatment in the allocation of quotas

The Anglo Latvian trade has developed considerably under the Agreement Latvia has increased substantially imports of British motor cars and accessories industrial machinery, pipes tools wool, woollen fabrics, and coal The exports of Latvian articles to the United Kingdom have also increased, particularly of bacon, butter, aspen logs, sleepers boxwoods, flax, plywood and paper Latvia enjoys a large favourable balance of trade with the U K Britain is the largest single market for Latvian goods,

Germany being the second. But as supplier to the Latvian market, the U K is a bad second to Germany German goods have acquired a firm hold over the Latvian market and offer very serious competition to imports from other countries Britain will, therefore, have to build up her business connections gradually

The trade agreement with Estonia is of similar type The Government of Estonia has reduced or consolidated import duties on a number of articles including mustard, pickles, sugar, spirits and strong alcoholic liquors, salt, fish, skin and leather manufactures, coal and coke, iron and steel, tin, musical instruments, cycles, motor cycles, motor vehicles, cotton yarn and fabrics, wool yarn and fabrics, etc Further, Estonia agreed not to impose fresh quantitative restrictions on certain articles British coal was accorded a quota of 85 per cent In return the British Government agreed to reduce and consolidate import duties on specified Estonian articles Besides, Estonia was guaranteed most-favoured-nation treatment in respect of quota restrictions

Anglo-Uruguayan Trade Agreement.—The trade agreement with Uruguay guarantees most-favoured-nation treatment in respect of commodity trade The Government of Uruguay also undertakes to maintain free entry for British coal But, as noted in the preceding section, the agreement is mainly concerned with exchange difficulties The agreement has helped materially the British bond holders

Trade Agreement with Yugoslavia.—In 1936, the Yugoslav Government, in order to correct adverse balance of trade, decided to control the imports from non-clearing countries. Accordingly, a list of commodities was published the importation of which from non-clearing countries was subject, as from June 25, 1936, to the granting of a licence by an Import Committee formed at the National Bank This list affected about 62 per cent. of the total imports from the U. K. This restriction had an adverse

effect on the British exports Therefore, the Anglo-Yugoslav Trade and Payments Agreement was signed on 27th November, 1936 Under the agreement the Yugoslav Government undertook to issue import licenses for the British goods on the restricted list up to certain prescribed values depending on the value of Yugoslav exports to the U K Under the import control system, however, the scope for the expansion of British exports to Yugoslavia is limited

Anglo-American Trade Agreement.—This Agreement signed in Washington in 17th November, 1938 effects some breaches in the scheme of British Imperial Preference [1] This is a very significant and valuable feature of the agreement American exports to the U K include both industrial as well as agricultural products The British tariff, particularly preferential tariff, had caused considerable consternation in the United States It was said that American farmers would not have found the British tariff on their wheat a serious obstacle to sales in the British market if the Canadian wheat had also paid the same duty But, with the Canadian wheat entering free of duty, the duty of 6 per cent on American wheat became a real hardship Similarly, the duty on rice would not have meant much if Indian rice was accorded similar tariff treatment The American farmers were also concerned with the British import duties on tobacco, barley, condensed milk apples, canned and dried fruits because of the preferential treatment accorded to competing producers within the British Empire The American manufacturers however, felt the hardship of preferential tariffs relatively much less due to their stronger competitive position as against the Dominions, resulting from their advanced technique of industrial production and the established commercial connections The United States therefore, rightly claimed that the Ottawa Trade Agreements should be suitably modified so

1 It is a landmark in the history of liberal formal bilateralism underlying the recent United States trade policy as distinct from the restrictive substantive bilateralism characteristic of German Commercial policy and in a lesser degree of many of the agreements made by the United Kingdom herself Vide Dr Madan B p 6 Credit for this healthy change in the British commercial policy must go largely to the United States

that her agricultural exports may enter the British market on the same terms as those from other Empire countries It was a protest against the exclusive Imperial Preference

Apart from the modification of the Ottawa Trade Agreements, the advantages which Britain could offer to the United States were limited So far as the commodities on the free list are concerned the American producers already enjoy full and unrestricted access to the British market No concessions could possibly be made here There is however another important group of commodities subject to duties, in respect of which Britain had made no commitments at Ottawa and is therefore free to reduce them In this list valuable but limited concessions could be made due to the comparatively low level of duties Substantial and useful concessions therefore could be made only at the cost of Ottawa agreements

The concessions accorded by Britain are embodied in Schedule I attached to the Agreement and cover about two-thirds of the American articles imported into the U K. The total American imports into the U K. amounted to about £93m in 1936 of which about £61m or 63 per cent are covered by the present agreement Duties are reduced on 11 per cent undertakings not to increase existing duties cover another 15 per cent, free entry is accorded to 12 per cent, while the remaining 17 per cent is given other concessions These concessions are determined by the formula of "principal suppliers" so that the benefits may be enjoyed primarily by the United States

The imports of American commodities on which duties are reduced were valued at about £11 2m in 1936 Duty of 2s a quarter on wheat is abolished with the consent of Canada Australia and India Important concessions are made on soft wood with the consent of Canada The duty on rice is reduced from 1d to 2/3d per lb On apples, cherries, finest juices duties have been reduced Grape fruit is placed on the free list Duties are reduced on the imports of American manufactures including various types

of machinery, metal manufactures, electrical goods, gramophones, typewriters, etc

The undertakings not to increase present duties cover primary raw materials as well as manufactured goods, including motor cars, agricultural tractors, dairy and other kinds of machinery, plywood, paraffin wax, celluloid, etc Britain agreed not to increase the present preference of about 2s a lb on unmanufactured Empire tobacco Free entry is maintained for some important raw materials such as sulphur, raw cotton, rosin, fur skins, etc

The Schedule of tariff concessions on British goods, accorded by the U S A contains 600 items The imports of British goods into the U S A in 1936 were valued at £40m of which £23m are liable to duty and the rest enter duty-free Of the dutiable class of goods, the present agreement secures duty reductions on £11m and existing duties are stabilised on £9½m Thus, of the total trade valued at £40m concessions have been accorded on £27m

In return valuable concessions are made on British cotton manufactures by the U S A For ' plain woven " cotton clothes with yarn of counts 31 to 50, the reductions amount to 48 per cent On unbleached cloth the minimum specific duties are reduced by 27 per cent For cotton yarns of counts exceeding 60 duty reductions are up to 20 per cent Duties on woollen manufactures have been substantially reduced American duties on woollen goods contain both specific and *ad valorem* elements *Ad valorem* duties are substantially reduced on the whole range of woollen piece-goods On linen manufactures, too valuable reductions are provided In the group of metal goods, substantial reductions are accorded on silver plated ware pens, cutlery, bicycles, machinery, etc The stabilisation of duty on whisky at the low level to which it was reduced by the Canadian-American Agreement of 1935 is important, for American imports of British whisky amounted to £5m in 1936 Duties on earthenware, china and glass are substan-

tially reduced Duty reductions have also been obtained on a wide range of miscellaneous goods

It will, thus, be seen that the formula of reciprocity has been punctiliously observed by the negotiators of the Anglo-American trade agreement in respect of duty reductions Nevertbeless, the concessions offered by the United States have provided a decisive increase in British competitive power and the British exports must therefore increase Besides the concessions have been very well distributed amongst the British producers

The British concessions are of a peculiar character The excessive protection extended to the domestic producer is untouched, he continues to be sufficiently safeguarded The most obvious result is tbat the competitive position of the American exports *vis-a vis* the British (domestic) producers remains unaltered, the domestic producer is still favoured All that the Agreement does is to reduce in certain cases the preference accorded to the Empire producers The result will be to divert certain amount of trade from Empire countries to American hands, without increasing the total volume of imports into Britain. The concessions are, however, welcome since they effect breaches into the system of Imperial preference built at Ottawa which has led to uneconomic diversion of trade But it should be remembered that the essential features of the extreme British protectionist policy remain intact Britain has tried to drive a valuable bargain at the expense of the Dominions and other members of the Empire, without making any tangible and substantial changes in the protection accorded to her own domestic producers Under these conditions the revival of world trade must necessarily be slow

The conclusions from the foregoing analysis of British commercial policy may now be summarised

(1) Since 1931, Britain has adopted a highly complex commercial policy, witb heavy domestic protection, quota restrictions on imports, imperial preference, etc, whicb bas

spurred the trend towards autarky and thereby led to unwarranted diversion and restriction of world trade

(2) Equipped with this new protectionist and discriminatory tariff, and unfavourable balance of trade, Britain has tried to find larger foreign markets for her manufactures through bilateral agreements Hard bargaining and bilateral balancing of trade has been resorted to

(3) The trade agreements have brought valuable reciprocal concessions in the form of duty reductions, conventionalisation of duties and the guarantees of free entry But sometimes concessions have been illusory due to tariff padding

(4) The discriminatory concessions obtained by Britain through these bilateral trade agreements have caused serious damage to international economic relations

(5) Genuine and lasting revival of world trade cannot be effected by narrow and discriminatory bilateral trade pacts At best, this type of bilateral trade agreements are mere expedients for tiding over temporary difficulties To be useful, therefore, these agreements must guarantee equality of treatment and prepare the way for multilateral trade agreements

(6) Britain, if it is to give the lead in improving the international economic relations, which her position demands, must radically alter her protectionist system and change the structure of her trade agreements The agreements must be shorn of the discriminatory elements and substantial concessions should be accorded to all those countries prepared to mould their commercial policy on sane and liberal lines Narrow economic nationalism must be discarded if the world is to be saved the spectre of economic and political disaster Britain must give prompt and courageous lead in the revival of world trade

CHAPTER X

INDIAN COMMERCIAL POLICY AND TRADE AGREEMENTS

In the preceding chapters we have analysed the technique of modern commercial policy as pursued by the more important industrial countries. The detailed analysis of commercial policy has revealed the important part played by the protectionist tariff in the development of modern industries. The new developments in the technique of protectionism, during the depression in particular, have relegated tariffs, as an instrument of commercial policy to the background and introduced considerable complications in modern commercial policy with disastrous consequences on world trade. In fact, the economic developments during the Great Depression have entirely revolutionised the technique of modern commercial policy. No country in the world could remain immune from the influences of these new developments in view of the closer economic interdependence. In many cases commercial policy had perforce to be changed in self-defence against the aggressive economic nationalism of other countries. In view of the important part that protection has played in the development of modern commercial policy and the revolutionary changes it has undergone during recent years it behoves us to examine the influence it has exerted on Indian commercial policy. In the present chapter, therefore, we propose to examine the nature of Indian commercial policy and its effects on the development of Indian as well as world trade.

Laissez Faire up to 1923.—Indian tariff policy has been a medley of incongruities formulated and worked to the utter disregard of national needs and aspirations. Protection, as shown in the preceding pages,[1] has played an important part in reshaping the industrial structure of the

1 Vide Chapter I.

world, though it has some obvious limitations Great Britain, the United States, Germany, France, and Japan, to take only a few illustrations, have had to resort to protection for reorganising their industries India, being a late-comer in the race for industrial reconstruction, ought to have drawn object lessons from the experience of these advanced industrialised countries The Government of India has, however, refused to learn, the lessons of modern economic history have been ignored in toto India has been made to follow a commercial policy inconsistent with her economic requirements For instance, the modern industrial structure of Britain is the fruit of very carefully thought out and planned protectionist commercial policy During the Industrial Revolution when the British industries were re-organised, protective tariff formed an integral part of British commercial policy By 1850 British industries attained full maturity and Britain became the workshop of the world At this stage of her economic development there was no need for protection Therefore Britain discarded protection and took to free trade, as required by the position she had come to hold in the industrial system of the world She needed free markets for the purchase of raw materials required by her manufacturing industries and for the sale of the finished goods turned out by them Britain continued to pursue this policy, with certain exceptions, up to 1931, when once again there came a relapse to protection The most disquieting feature of Indian commercial policy throughout the pre-war period was that the Government of India failed to protect or aid the indigenous industries against the unfair competition of well-established foreign industries Throughout the pre-war period India was made to follow the policy of free trade though her essential economic requirements, in view of her backward industrial structure in face of plentiful natural resources and wide home market, warranted a reasonable protectionist policy Throughout this period of over sixty years Indian tariff was essentially a revenue one Even a purely revenue tariff was tolerated by the British commercial interests with

considerable reluctance Thus, whereas Britain had followed a commercial policy more or less in keeping with her economic requirements, India was denied a national commercial policy

The financial burden imposed by the Great War necessitated an enhancement of tariff In 1916, the general rate was raised from 5 to 7½ per cent The exemptions were curtailed Import duty on sugar was raised to 10 per cent The duties on liquors and tobacco were also raised substantially In 1917, India made a special War Contribution of £100 m to the Imperial Treasury which made fresh taxation imperative[1] Therefore the import duty on cotton piecegoods was raised to the general level of 7½ per cent, the excise remaining unchanged at 3½ per cent Other duties were also raised These high revenue duties had a bracing effect on Indian industries To this must be added the sharp curtailment of foreign imports, due to the concentration of production in belligerent countries for supplying military requirements, shortage of shipping facilities and the vigorous submarine activities conducted by Germany The absence of foreign competition led to the expansion of Indian industries This was not all To this accidental assistance must be added the invaluable direct help given by the Government of India in stimulating the production of war materials In order to supply the eastern theatres of war with military requirements, the Government of India appointed a Munitions Board to look after the key industries No wonder, therefore, that during the war, even though tariff was not used as an instrument of industrial protection, the Indian industries recorded remarkable growth In short, the Great War unequivocally demonstrated the industrial potentialities of India which can be easily brought to fruition under a suitable protectionist tariff

With the declaration of armistice and resumption of normal commercial relations the inroads of foreign imports

recomenced Besides, after the War Japan emerged as a fresh and strong competitor in the field of industrial production The withdrawal of natural protection afforded by the War caused an immediate setback in our industrial development The Indian Munitions Board, which had rendered invaluable assistance to Indian industries during the War, was also disbanded The revenue tariff was, however, raised to meet the financial deficit The general rate of duty was raised from 7½ per cent to 11 per cent in 1921 and to 15 per cent in 1922 The import duty on cotton piece-goods was raised to 11 per cent while the excise duty remained unchanged at 3½ per cent This gave valuable protection to the domestic cotton mill industry The duty on sugar was raised from 10 to 15 per cent in 1921 and to 25 per cent in 1922 Luxury articles were subject to a duty of 20 per cent in 1921 which was raised to 30 per cent in 1922 In short, in 1922, the tariff had recorded remarkable changes as compared with the pre-war period The reliance on customs revenue had increased considerably It should however, be noted that the tariff was entirely a revenue one, dictated by the necessity of balancing the budget, the need for a protective tariff suited to the industrial requirements of the country had not been clearly realised by the Government of India Nevertheless, the protective element was imperceptibly creeping in The export duty on raw hides and skins was imposed in 1919 for protecting the Indian tanning industry This export duty, on hides and skins, introduced the novel principle of Imperial preference in the Indian tariff policy, by providing for a rebate of two-thirds of the duty in the case of hides and skins exported to the Empire and tanned there

Apart from these changes, public opinion in India had incessantly demanded an expert examination of the tariff policy and its revision to suit the peculiar economic conditions in India The question of fiscal policy had been excluded from the terms of reference to the Industrial Commission in 1916 on the ground that the question of protection could not be considered during the war This exclusion, as the Montague-Chelmsford Report admits, was

the object of legitimate criticism in India The need for a change in Indian commercial policy received wider recognition [1] The Joint Select Committee in 1919 outlined the convention of fiscal autonomy for India as under

> Whatever be the right fiscal policy for India for the needs of her consumers as well as for her manufacturers it is quite clear that she should have the same liberty to consider her interests as Great Britain Australia New Zealand Canada and South Africa In the opinion of the Committee the Secretary of State should as far as possible avoid interference on this subject when the Government of India and its Legislature are in agreement and they think that this intervention when it does take place should be limited to safeguarding the international obligations of the Empire or any fiscal arrangement within the Empire to which His Majesty s Government is a party '

To meet the insistent demand of the public in India for a revision of the tariff policy the Fiscal Commission was appointed in 1921 with Sir Ibrahim Rahimtoola as its chairman to examine with reference to all the interests concerned the tariff policy of the Government of India, including the question of the desirability of adopting the principle of Imperial Preference and to make recommendations

As regards the industrial development of the country, the Fiscal Commission *found that it had been limited and slow* They endorsed the conclusion drawn by the Industrial Commission that "the industrial system is unevenly, and in most cases inadequately developed, and the capitalists of the country, with a few notable exceptions, have till now left to other nations the work and the profit of manufacturing her valuable raw materials or have allowed them to remain unutilised" It was accepted that adequate development of suitable industries would be very much to the advantage of the country as a whole, creating new sources of wealth, encouraging the accumulation of capital

enlarging the public revenues, providing more profitable employment for labour, reducing the excessive dependence of the country on the agriculture and finally stimulating the national life and developing the national character [1]

The Policy of Discriminating Protection since 1923-24.— The policy of protection was unanimously recommended as more suitable for the industrial development of India Both the Commission was divided on the question of the application of the policy of protection The Majority Report outlined a policy of protection to be applied with discrimination along certain lines Let us note, in brief, the details outlined by the Commission The scheme of discriminating protection was to be worked with the assistance of a Tariff Board, so that before an industry could be awarded fiscal protection it should establish its claim to the satisfaction of the Board The Board after detailed investigation into the economic conditions of the industry is to recommend whether protection should be extended and, if so, the precise rate at which protection may be given The Commission laid down following tests, as conditions precedent, to be fulfilled, to the satisfaction of the Tariff Board, by an industry claiming protection Firstly, the industry must be one possessing natural advantages, such as abundant supply of raw materials, cheap power, a sufficient supply of labour or a large home market Secondly, the industry must be one which without the help of protection either is not likely to develop at all or is not likely to develop so rapidly as is desirable in the *interests of the country Thirdly, the* industry must be one which will eventually be able to face world competition without protection Certain exceptions have been laid down under which an industry may be granted protection even if it fails to satisfy the aforesaid principles An industry which is essential for national defence and for which conditions in India are not unfavourable, should if necessary, be adequately protected, irrespective of the conditions laid down above Further, protection to basic industries should be determined by considerations of national economics

1 Vide Para 54

The Minority Report, however, did not approve of this sort of policy of discriminating protection and stressed in unqualified terms that the fiscal policy best suited for India is protection They supported a policy of intense industrialisation "While we agree," says the Minority Report, "that the policy of protection should be applied with discrimination, we do not think that any qualifications or limitations should be made a condition precedent to its adoption The conditions laid down in the Majority Report are stringent and will delay the pace of industrial expansion" Thus, the Commission was unanimous in recommending that the policy of discriminating protection[1] should be adopted, but they differed as to the qualifications to be imposed on the application of the policy

It is generally agreed that the policy of protection should be applied with discrimination Indiscriminate protection of all Indian industries would lead to waste There should be a reasonable chance for the industry seeking protection to be able to face world competition without protection in the near future, except where the industry is essential for national defence Protection should essentially be temporary The other tests laid down by the Majority Report of the Fiscal Commission, as conditions precedent to be fulfilled by an industry claiming protection, are rigid. Of course, much depends upon way in which these conditions are interpreted The rigidity of the conditions would be materially relaxed if a liberal interpretation is put by the Tariff Board But a strict interpretation would seriously retard the industrial development of the country Besides, for an industrially backward country it is undesirable to put these rigid conditions and fetter thereby the discretion of the Tariff Board For instance, it is not always neces-

sary that an industry seeking protection should show an abundant supply of raw materials The structure of the Lancashire cotton industry shows us beyond doubt that an efficient industry can be organised without an abundant supply of raw materials" Lancashire cotton mills import their raw cotton from the distant countries like the United States Similarly the Japanese cotton mill industry draws its raw cotton from India and the United States. The jute mills at Dundee depend for their raw material on jute imported from India And yet these industries compete successfully with the Indian industries in India Such cases can be multiplied Similarly "a large home market is not always an essential pre-requisite of an efficient industry If these conditions were imposed by Britain, Japan, Germany etc most of the organised industries would have been nipped in the bud and the world would have been poorer today Most of these advanced countries have followed a strong protectionist policy with a view to promoting a rapid industrial development of the country In the first chapter we have shown the part played by protectionist commercial policy in the industrial development of the more important industrialised countries Thus, some of the conditions imposed by the Fiscal Commission are rigid and unwarranted by the experience of other countries These conditions should therefore be more liberally interpreted.

Machinery of Protection.—The establishment of a competent and impartial Tariff Board is an integral part of the scheme of discriminating protection outlined by the Indian Fiscal Commission, which is to enquire into the conditions of industries and recommend whether protection should or should not be extended to them and if extended, what the rate of protection should be Needless to add that the success of the scheme depends upon the efficiency of the Tariff Board. The most essential requirement is that the Board must be a permanent body [1] so as to secure consistent

decisions and continuity of policy The importance of a continuous and consistent commercial policy, free from sudden and violent changes, cannot be over stated In the absence of an assurance provided by such a policy, the protected industries would not attract sufficient capital and enterprise essential for rapid and ordered industrial development In the case of industrially backward countries a relatively stable protective tariff is of greater importance Besides, a permanent Tariff Board will command better expert technical knowledge and will be able to maintain more disinterested and detached attitude in making recommendations than a temporary *ad hoc* Board The security of tenure must therefore be assured

The Indian Tariff Board is an *ad hoc* body, appointed by the Government of India to investigate the claims of a particular industry for protection and report thereon to the Government The Board is constituted for each enquiry with specific terms of reference Thus, the most important recommendation of the Fiscal Commission for a permanent Tariff Board has been ignored by the Government of India. The experience of other advanced countries has shown the importance of a permanent Tariff Board The Government of India has, however, thought it expedient to experiment with the temporary Board The consequences of this temporary tenure are far-reaching and vicious The members who are not guaranteed security of tenure, naturally, try to placate the Government of India It is idle to expect of the members of an essentially temporary Board, with prospects of lucrative posts of power and prestige awaiting them,[1] to sit on judgment over the rival British and Indian claims dispassionately Impartial outlook under these conditions is a mere illusion Besides, it is very difficult to get the services of "thoroughly competent" people to work on a temporary Board No wonder if the Indian Tariff Board or Boards have failed to inspire confidence in the general public

Even if it were possible to get the services of competent and impartial members to work on the Board, it is undesirable to have a temporary Board for another important reason It has already been said that the value of the *recommendations* of the Board would largely depend upon the definite and detailed information it can get affecting the costs of production This invaluable information can be had only on adequate assurance of preserving utmost secrecy For securing secrecy it is essential that the members of the Board should be debarred from joining business [1] or any other service, after they have severed their connections from the Board Where the Board is temporary this condition, otherwise essential and invaluable, would be a serious hardship on the members The Government of India have, therefore, been unable to impose this restriction The most obvious result is that the manufacturers have on several occasions flatly refused to divulge confidential information [2] Even where the formation has been given under the present conditions its accuracy and value must necessarily be doubted [3] The blame for this state of affairs rests primarily with the Government of India The manufacturers are right in refusing to disclose confidential data relating to their industry when the same can be easily placed at the disposal of rival firms

The functions of the Tariff Board should be fairly wide The Board should study generally the effects of our commercial policy as a whole and suggest suitable changes to the Government of India The Fiscal Commission[4] rightly suggested that the Tariff Board should investigate the claims of particular industries for protection, watch generally the

effects of the measures of protection,[1] report on the nature of Imperial Preference that India may accord in her national interests, to watch generally the effects of tariff policy, etc Further, the Tariff Board should make a correct estimate of the direct and indirect costs of any measure of protection it may recommend.

The powers of the Tariff Board, appointed by the Government of India from time to time, have been strictly limited The Board has had to investigate only those applications for protection which were referred to it by the Government of India The scope of investigation is also strictly limited by the terms of reference This restriction limits the value of the enquiry and the recommendations are also strictly limited by the terms of reference Besides, the Board has not been given power of compelling the parties to produce the necessary data, which they otherwise refuse to place before it The Tariff Board has, therefore, often to base its recommendations on secondary data, which impairs considerably their accuracy

In this connection the experience of the Australian Tariff Board is instructive The Minister of Trade and Customs has to refer to the Board for enquiry and report matters relating to (1) classification and valuation of goods, etc; (2) proposals for new increased, reduced or deferred duties, (3) granting and effects of bounties, (4) the intermediate and preferential schedules, (5) any complaints against manufacturers abusing the State aid afforded to them by the tariff, (6) the general effects of the working of the Customs and Excise Tariff on the industries of the country, (7) the fiscal and industrial effects of the Customs Laws, (8) the relative effects of the duties on raw materials and on finished goods (and partly finished goods), and (9) any other matters affecting the encouragement of indus-

tries The Board is empowered to recommend after a careful enquiry into the conditions of an industry, about which a complaint is made, that the amount of duty payable to its commodities be abolished or reduced or that such action might be taken as the Board deems fit. The Board is empowered to enquire and report on its own initiative on any matters relating to subjects in (6) and (9) above Thus the powers of the Australian Tariff Board are fairly wide and it has initiative in certain respects

The practice of vesting the initiative in respect of investigation with the Government of India is both dilatory and dangerous It is dilatory because an industry seeking protection has to satisfy the Commerce Department as regards the validity of its claim before it can be referred to the Tariff Board for enquiry If the Commerce Department carefully scrutinises the complex details of the claims and bases its decision on the data placed before it, the procedure entails needless duplication of effort If the data is not carefully scrutinised, the practice requiring the detailed data to be produced before the Commerce Department is apt to cause needless delay and vexation Again, if the Commerce Department declines to refer a claim for investigation to the Tariff Board without a full study of the data placed before it, the industry would be denied its elementary right and the industrial development of the country retarded thereby The present practice is dangerous because *the discretion vested in the irresponsible* Executive may not be judicially exercised. There is no appeal against its arbitary use It cannot therefore, be too strongly stressed that if the public is to make full use of the Tariff Board the initiative in respect of investigation must rest with the Board The Board may, however, require a deposit from the applicants, which may be forfeited if the claim is found to be frivolous This provision would effectively eliminate vexatious claims from being referred to the Board

The need for utmost publicity of the work of the Tariff Board has been accepted. The Indian Fiscal Commission

also laid due emphasis on this point The experience of other advanced countries like the United States, Australia, Canada, etc, supports this contention The Fiscal Commission held that the Tariff Board should hold the formal enquiry in the public and that all possible interests be given full opportunity for representing their point of view before the Board Of course, the whole investigation need not be held in public This is an invaluable safeguard for businessmen For instance, when evidence is being led about the cost of production it is essential that utmost secrecy be preserved about the information thus placed before the Board Without this protection the manufacturers would rightly be reluctant to divulge the information And without authentic and precise data it would be impossible for the Board to make any definite and detailed recommendations To secure this objective mere holding of the investigation in camera is not sufficient The industrialists should have sufficient protection against the information leaking out from the hands of the members of the Board The Report of the Fiscal Commission is, unfortunately, silent on this point It should be noted that in the absence of definite and detailed information about costs of production the recommendations of the Board would have limited value Subject to this condition, the work done by the Board should be given wide publicity, so that the public may be able to form its own judgment The Fiscal Commission said that the Government should publish the results of the enquiry promptly, whether it agrees with the conclusions of the Board or not To give full publicity one feels that the Reports of the Board be published in local languages as well Publicity would minimise corruption and inspire confidence in the general public

The Tariff Board holds enquiries in public and submits the results of its investigations in the form of a report to the Government of India The Fiscal Commission recommend that "the Government should publish the results of the enquiry promptly, whether it agrees with the conclusions of the Board or not" The prompt publication of the Report, the Commission rightly thought, would inspire

needed for formulating a national economic policy and not merely conduct enquiries on claims for protection of specific industries Investigation of claims for protection should only be a part of its business Its more important function should be to place definite suggestions, based on its detailed studies affecting the economic policy of the country before the legislature for approval These studies should be published As regards the enquiries for protection, they should be more thorough and based on fuller data Both direct and indirect costs of protection should be definitely ascertained and the interests of consumers given due weight The Board should also state the time-limit within which an industry to be protected would be able to dispense with protection The Board should keep a watch over the working of the protected industries to see that they keep themselves abreast of the most recent developments and maintain their equipment at the highest pitch of efficiency If maximum efficiency is not maintained, protection should be withdrawn

Policy of Discriminating Protection Retards Rapid Industrial Development

Indian Glass Industry.—The case of Indian glass industry is interesting it illustrates the rigidity of the conditions imposed by the Fiscal Commission and the arbitary rejection of the recommendations of the Board by the Government of India The Tariff Board in the course of its investigations, found that there were ample deposits of sand, sandstone or rock suitable for use in the manufacture of glass and that the sand used in Indian glass works was obtained from the deposits in the country Indian sand by suitable treatment could be used for the manufacture of the best glass Sand represents the largest proportion of the raw materials used Soda ash which constitutes 25 per cent of the raw materials used, was imported. In 1927, when an application for protection was made by the glass industry, the Government of India had suggested that the industry could not be said to enjoy any natural advantage so long as it was dependent on imported soda ash But the second Tariff Board adopted a more liberal attitude in

interpreting the condition laid down by the Fiscal Commission and held that even if the industry was confined permanently to the use of imported soda ash the claim for protection could not be rejected unless it was found on balance that the industry did not possess sufficient natural advantages. Limestone was available in abundance Coal of good quality could also be bad Labour supply was cheap and abundant There was no shortage of skilled labour The inferior quality of much of the glassware made was due not so much to lack of skill on the part of the workmen as to lack of organising ability on the part of the management As regards the market the Board found that apart altogether from plate glass scientific glassware the best tableware and electric bulbs which the Indian industry did not attempt to make there was in India a market sufficient not only to absorb the whole of the production of the factories then in existence but also to encourage the establishment of new factories [1] There are also opportunities for export Besides a substantial expansion in the demand for glassware in India in future can be expected as the consumption is likely to grow They also found that the industry was faced with unfair competition against which it needed protection If suitable protection is given the industry would eventually be able to face world competition In view of these findings they made detailed recommendations for protection The Board submitted its report in 1932 but its publication was delayed for about two years Besides the Government of India rejected the recommendations of the Board

Electric Wire and Cable Industry—The claim of electric wire and cable industry for protection was turned down by the Tariff Board on the plea that it failed to satisfy the conditions laid down by the Fiscal Commission The investigation showed that there was very wide home market The maximum capacity of the Indian works is well within the total market available in the country Besides the consumption of electric wires and cables is rapidly increasing in India and there is a fairly good scope for the

[1] Vide Report, Para. 6

expansion of home market in future Sufficient labour supply was also available The power employed in the works was electric power of which sufficient supply was available for the maximum requirements of the company The important raw materials used were electrolyptic copper rod, lead and raw rubber Of these raw material, was, however, imported. The Board found that necessary supplies of copper were not available and that unless a market for 3,500 tons was definitely assured and the price of electrolyptic copper rod rose considerably higher, there was no likelihood whatever of electrolyptic copper rod being manufactured in India Therefore it was held that the Indian Cable Industry did not satisfy the first condition laid down by the Fiscal Commission.

Magnesium Chloride Industry.—The Fiscal Commission had rightly laid down the condition that an industry seeking protection must eventually be able to face world competition without protection But in the case of an industrially backward country like India this condition ought to be liberally interpreted in its application, lest it should cripple industrial enterprise In practice, as a result of strict interpretation of this condition protection was refused to some important industries which would easily have secured State assistance even in industrially advanced countries like the United Kingdom or the United States The Report of the Tariff Board on the Magnesium Chloride Industry of 1925 is very instructive in this connection In the pre-war period Germany enjoyed almost a monopoly of the world's production of magnesium chloride Being bye-products, the German manufacturers can afford to sell them at exceptionally low prices During the war, when the German supplies were cut off, there was a serious shortage of magnesium chloride in India and prices rose rapidly The manufacture of magnesium chloride was, therefore, started in 1916 at Kharaghoda For the fix six years the company was "exceedingly prosperous" In 1922, however, the prices of German supplies dropped heavily

so that by the end of the year the factory had to be closed Thereafter application was made for protection The Tariff Board found that the supplies of raw materials were enormous and far in excess of the quantity necessary to meet the total requirements of India Labour was also cheap and plentiful The quality of magnesium chloride made at Kharaghoda was found to be satisfactory The Board, however, refused to recommend the grant of protection on the plea that it was doubtful if the industry could eventually exist without protection in face of German competition This is a special case where an Indian industry had to compete with a foreign monopoly, which had control of the world market The German monopoly could easily dump supplies in the Indian market to oust out her Indian competitors These considerations ought to have been taken into consideration in determining the claim for protection Where an industry has to compete with a well-organised monopoly, with greater resources and wider markets, the period within which the domestic industry may be able to face competition unaided is apt to be longer Further, competition to be faced must be fair In short, the magnesium chloride industry, which possessed all the natural advantages, should not have been denied protection on the ground that it could not face the competition of German monopoly The right policy is to recognise this industry which possesses all natural advantages on proper lines so as to improve its efficiency, strengthen its financial resources by State aid and help to lower the cost of production Thus a liberal interpretation of the condition, adequate state assistance and effective supervision and regulation of the protected industries are essential for an efficient and rapid industrial development of India

From these few stray illustrations it will be seen that the rigid conditions imposed by the Fiscal Commission, strict interpretation by the Tariff Board and arbitrary actions of the Executive have all conspired to retard a more rapid development of Indian industries Some of the most important industries have been denied State assistance on the plea that they do not fulfil the conditions laid down

by the Commission It has already been shown that most of the advanced countries have organised their industries under strong tariff walls unfettered by rigid conditions The economic development of these countries briefly reviewed in the first chapter is an invaluable guide in moulding the commercial policy of industrially backward countries It shows us that these rigid conditions are needless and inimical to national interests It is possible to develop sound and prosperous industries with the aid of protection even though they do not strictly satisfy the rigid conditions laid down by the Majority Report of the Fiscal Commission For instance the British cotton textile industry could not have grown up if the British Government had refused protection on the plea that the most important raw material cotton had to be imported Today the Lancashire cotton industry imports raw materials from distant countries and exports its finished products to distant foreign markets and is still reckoned as one of the most important British industries The Japanese cotton industry likewise depends on imported raw cotton and foreign markets for its finished goods and yet it is one of the most efficient industries of the world Same is true of some of the other leading industries of the world In other words if Britain had based her commercial policy on these rigid conditions she could not have become the workshop of the world by 1850 Her industrial pre eminence is due largely to the prompt and effective policy of protection which led to rapid and intense industrialisation of the country The fears of the Minority Report of the Fiscal Commission that these conditions are stringent and that they will delay the industrial development of the country have come true

Arbitrary Rejection of Tariff Board Findings—This is not all At times the Government of India has arbitrarily rejected the recommendations of the Board without placing the same before the Indian Legislature The case of glass industry is most conspicuous The Government of India delayed the publication of the Report for two years and rejected the proposals of the Board In several cases the

Government have accepted the recommendations of the Board only in parts For instance, the Government of India refused to accept the unanimous recommendation of the Board on Cotton Textile Industry, 1927, about the imposition of an additional duty of 4 per cent on all cotton manufactures They also rejected the proposal for a bounty on the spinning of finer counts 32s and higher Only after a strong agitation the Government modified their decision and agreed to impose a duty of 5 per cent *ad valorem* or 1½ annas a pound, whichever was higher, on all imported cotton yarn In the case of the Heavy Chemical Industry, the Board recommended, *inter alia*, that railway rates be reduced in order to facilitate the formation of a combine But the Government declined to accept this recommendation Similarly, the Tariff Board in their report on Paper Industry recommended that Government should assist the industry by an advance of capital to the Indian Paper Pulp Company from their own resources or by the guarantee, in respect of both principal and interest, of a public issue of debentures in order that the possibilities of manufacture of paper by the sulphite process might be fully explored Further, they recommended that the Karnatic Paper Mills which intended to make paper from bamboo by the soda process, might also be assisted with capital in the same manner as the Indian Paper Pulp Company provided the Technical Advisors of the Government of India were satisfied that the scheme had reasonable prospects of success The Government however refused to give financial assistance and instead extended the period of protection recommended by the Board from five to seven years

Industrialisation under the Policy of Discriminating Protection—Notwithstanding the rigid conditions imposed upon the application of the policy of discriminating protection, some Indian industries have received invaluable assistance and recorded marked growth Indian steel industry has expanded considerably with the aid of protection In certain branches protection is dispensed with and the industry is able to face world competition Sugar industry has also recorded rapid expansion under the spur of tariff

protection. The number of mills producing sugar increased from 32 in 1931-32 to 154 in 1937-38 and the output of sugar from 158,581 tons to 10,50,000 tons during the same period. The imports of sugar declined from 511,319 tons in 1931-32 to 20,000 tons in 1937-38. Indian match industry has also progressed rapidly and today India has become self-sufficient in respect of her match requirements. The domestic industry supplies the whole market. Protection has been dispensed with. The match industry now faces world competition without the aid of protection. The development of paper industry has also been encouraged under the spur of protection, although the help given was inadequate. Indian cotton mill industry would have suffered a great deal in the absence of tariff protection it has hitherto enjoyed.

Need for a Bolder Policy of Industrialisation.—These few illustrations clearly show that even a half-hearted and halting policy of protection can help the industrial expansion of an industrially backward country. If the policy had not been hedged with the rigid conditions and the protection extended was adequate and prompt, the industrialisation of the country would have been more rapid. This does not mean that the Government of India should have extended protection indiscriminately to all industries claiming protection. Indiscriminate protection would be both wasteful and dangerous. Protection must be extended only after careful and detailed investigation of its implications by an expert body, which we call the Tariff Board. What we want is that protection to be successful should be adequate and prompt. The Government of India should, therefore, apply the policy of protection with sufficient boldness and discrimination. The rigidity of the conditions, discussed above, should be relaxed.

The progress, though limited, which Indian industries have made under the policy of discriminating protection is due largely to the liberal interpretation put in certain cases by the Tariff Board on the conditions imposed by the Majority Report of the Fiscal Commission. For instance,

in the case of match industry it was found that India did not have an abundant supply of raw materials but the Tariff Board waived the condition on the ground that no country in the world was self supporting in regard to all or most of the raw materials Similarly in the case of paper industry the conditions were liberally construed It was found that the supply of sabai grass the most important raw material used by the Indian paper mills was both limited and unsatisfactory so that the industry could not strictly be said to possess an abundant supply of raw materials Besides with the unsatisfactory supply of raw materials it was not likely that the paper mills could dispense with protection in the long run as required by the third conditions But the Tariff Board felt that the bamboo pulp industry had a great future and if it was properly developed India would then be able to provide the important raw materials to her paper mills and have a surplus for export On this plea the Tariff Board recommended protection

Imperial Preference—Apart from the rigid conditions discussed above with which the policy of discriminating protection is hedged the adoption of Imperial Preference by the Government of India as an integral part of our commercial policy has militated against the rapid industrialisation of the country It has been shown that in the second half of the nineteenth century with the growth of industries in Europe and America British manufacturers were faced with increasing competition in foreign markets This competition grew and assumed a serious form in the last decade of the nineteenth century The aid of Imperial Preference was therefore sought as an escape from the otherwise difficult situation The dangerous implications of this change in commercial policy were probably not realised in full by its sponsors then The policy of extreme economic self sufficiency and growing economic imperialism which have restricted world trade and constitute a serious menace to world peace are in no small measure due to the exploitation of imperial sentiments for narrow self inte

very much less in need of preference than do manufactures, and that the gain to them by preference is likely to be correspondingly smaller With regard to foodstuffs, the general tendency in most countries is to admit them free and the possibilities of preference are limited "[1]

The Commission carefully examined the preference granted to Indian products in the U K and came to the conclusion that "Indian exports are not capable of benefitting to any great extent by preferential rates, particularly such as can be granted in the United Kingdom" Even if British tariff policy was modified with a view to extending the field of preference, they held that the gain to India would not be great Both the actual and possible gain that India may derive from preference in the British market is small *Per contra*, India can accord valuable tariff preference to British imports But such preferences would impose a serious burden on the Indian consumers The Commission agreed that it is unreasonable to ask the Indian consumer to bear an appreciable burden for the benefit of British manufactures "Such burden as appears to us inevitable in the pursuit of a policy of more rapid industrial development the Indian consumer may be asked to bear But he should not be called upon to bear an additional burden on top of this for the furtherance of interests which are not primarily Indian They also admitted that ' any considerable application of a policy of preference would cause distinct economic loss to India ' Thus a study of the Majority Report of the Fiscal Commission reveals that the policy of Imperial Preference is definitely injurious to Indian interests

Finding that the policy of Imperial Preference was definitely against the economic interests of India the Fiscal Commission recommended that India should adopt this policy "as a test of loyalty to the Empire They said "Imperial Preference is regarded throughout the Empire as a means of strengthening the ties which bind together

1 Vide Para. 233.
2 Vide Para 243

its scattered units We would not have India standing in a position of moral isolation within the Empire" India was, therefore, expected to help to maintain the prosperity of British export trade as a member of the British Empire

The Majority Report of the Fiscal Commission however, held that the policy of Imperial Preference should be adopted only with the free consent of Indian public opinion "The Indian view," they held "can be best ascertained by reference to the Council of State and the Legislative Assembly without whose free consent no such policy can be adopted" The Commission also laid down certain principles which should govern the application of the policy, if adopted Firstly, no preference should be granted on any article without the approval of the Indian Legislature Secondly, no preference given should in any way diminish the protection required by the Indian industries[1] Thirdly, the preference should not involve any appreciable economic loss to India after taking into account the economic gain which India derives from the preference granted her by the United Kingdom Fourthly before the Legislature is asked to pronounce an opinion on the policy, the Tariff Board should carefully examine the case of each individual commodity in the light of the aforesaid principles No preference should be to the detriment of Indian interests

It is essential to note that the adoption of the policy of Imperial Preference was advocated by the signatories of the Majority Report only in their individual capacity, without any backing of public opinion in the country The entire public opinion was definitely against the adoption of any such policy The Report itself admits "the almost complete unanimity with which the Indian witnesses opposed the principle of Imperial Preference" India was therefore, in no way committed to the policy of Imperial Preference

Preference within Protection Steel—Notwithstanding the marked hostility of Indian public opinion against any

form of Imperial Preference the Government of India has gradually led the country into it Two important Indian industries steel and cotton, will be reviewed here by way of illustrations The system of preferential duties in favour of British manufacturers was first introduced by the Steel Industry (Protection) Act of 1927 The Tariff Board in its enquiry on Steel Industry in 1927 had recommended a system of differential duties higher duties on Continental and lower duties on British steel A system of uniform duties it was argued would impose a heavier burden on the consumer of standard British or Indian steel than a system of differential duties The Board held that a *system of differential duties is desirable in the interests of* India on economic grounds for the adequate protection of Indian industries and after a fair adjustment of the burden involved [1] To remove the impression that a system of differential duties in the form suggested involves the *adoption of Imperial Preference in relation to steel* the Board laid down that these proposals do not imply a definite decision on the question of policy

The differential duties on iron and steel were further altered by an agreement supplementary to the Indo British Trade Agreement of 1932 signed at London in September 1932 The Indian Delegation was anxious to find out adequate outlets for Indian pig iron for its export markets had tended to decline They thought that exports of Indian pig iron to Japan had an uncertain future for Manchuria was expected to supply the Japanese demand Therefore *attempts were made to secure the British market* Further the Delegation felt that they could secure additional market for substantial quantities of Indian sheet bars and billets in the United Kingdom since Britain had imposed an import duty of 33 per cent on foreign steel in June 1932 The duty was *expressly protectionist in purpose intended* to improve the efficiency of British steel industry and encourage home production to fill the gap caused by the exclusion of Continental imports The Indian Delegation

1 Vide Report of the Tariff Board 19 Para 10
2 Ibid.

however, was under the belief that "if agreement could be reached with the British Government, Indian steel and pig iron would replace much of the continental material" Even this meagre and indefinite concession could not be had without offering additional advantages to the British manufacturers in the Indian market Since the protected classes of steel could not be touched, the additional advantage was accorded to galvanised steel sheets The differential duties agreed to were as follows (i) Rs 30/- a ton on sheets made in the United Kingdom from Indian sheet bars (ii) Rs 53/- a ton on sheets made in the United Kingdom from other sheet bars (iii) Rs 23-12-0 a ton on sheets made in the countries other than the United Kingdom

In case non British sheets were imported at lower prices additional duties were promptly imposed in order to maintain the level of prices These terms were embodied in an agreement which came into force from January 1st, 1933, and were to remain in force until the recommendations of the next Tariff Board on the Iron and Steel Industry were enforced This Agreement was claimed by the Delegation to be advantageous to both the countries In practice it was found to be cumbrous and conferred only limited benefits on the parties The representatives of the British Steel Industry, therefore showed their reluctance to renew the agreement The Indian Tariff Board Report of 1934 on Iron and Steel Industry laid down that the Agreement had served its purpose and its renewal was not desirable The Agreement was, therefore, not renewed.

It is surprising to find the Tariff Board recommending preferential duties on British galvanised sheets imported into India, notwithstanding the refusal of the British manufacturers to accord favoured treatment to Indian steel bars The Board argued that the system of differential duties embodied in the Steel Industry (Protective) Act of 1927 had worked quite smoothly without entailing any hardship either to the steel industry or consumers, and they saw therefore no reason to consider any change in the system.

It must, however be noted that differential duties were never imposed on galvanised sheets by the Act of 1927, nor were any such duties recommended by the Tariff Board of 1930 which was especially authorised to investigate the case of galvanised sheets These differential duties were for the first time imposed by the Iron and Steel Agreement of 1932 Further, since the British Steel Industry had declined to be a party to this Agreement characterising it as a wasteful and unsound there was no necessity for Indit to accord tariff preference on British galvanised sheets The Tariff Board of 1934 however, recommended a duty of Rs 10/ per ton on British sheets and Rs 40/- on non British sheets imported into India in order to maintain the principle of reciprocity agreed upon the Ottawa In support of this case the Tariff Board argued as follows

The duties under our scheme of protection are based generally on the current market prices of British and Continental steel In the case of galvanised sheets however we have estimated the duties on a different basis Since November 1923 the price of galvanised sheets has been fixed at an artificial level under the Ottawa Agreement No direct information is therefore available regarding the level of market prices under ordinary competitive conditions and our estimate of market prices has in consequence to be based on somewhat arbitrary considerations Two arbitrary methods have been open to us first to take the average price in the early half of 1932 and adjust it for the variation in the price of spelter since that period and secondly to proceed on the basis of calculation adopted by the Ottawa Delegation namely to take the United Kingdom price at the lowest figure which the Delegation considered would give a reasonable return to the British manufacturer and to take all continental prices at the lowest figure actually reached in recent importations Under ordinary conditions we should be inclined to adopt the first method in estimating the measure of protection The United Kingdom prices in the case should be almost the same as continental prices and there would be no scope for differential duties We have however decided to adopt the other method which is calculated to give the British manufacturer a definite advantage consistently with the interests of the industry Our object in doing so is to maintain as far as it is now possible the principle of

reciprocity underlying the Ottawa Agreement relating to galvanised sheets "[1]

Thus, the Board admitted "that there was no scope for differential duties" And yet they were anxious "to give the British manufacturers a definite advantage" consistent "with the interests of Indian industry" This sort of reasoning lacks clarity Discriminating protection being the accepted policy of the Government of India, it is the primary duty of the Tariff Board to accord adequate protection to Indian industries Discriminatory treatment should be scrupulously avoided Besides, it is difficult to get precise information about the cost of production of foreign manufacturers If, therefore, the duty of Rs 40/- per ton was found to be just adequate to protect the domestic industry, the concession of Rs 30/- per ton offered to the British manufacturer cannot be said to be "consistent with the interests of the Indian industry" In short, Indian steel industry got inadequate protection It must impair efficiency of the industry and prolong the period of protection This is rather a heavy price to pay for the so-called Ottawa spirit of reciprocity Besides, there was no case for the spirit of reciprocity in view of the attitude adopted by the British steel manufacturers In short, the preference in favour the British steel manufacturers was unwarranted on economic grounds The duty should have been uniform

These lower preferential duties recommended by the Tariff Board on British steel imports have been detrimental to the interests of Indian steel industry, Indian consumers and the revenue of the Government of India There was a considerable diversion of trade, the continental suppliers of steel to India were replaced by the British manufacturers This diversion of trade has been admitted by His Majesty's Trade Commissioner in India In his Report for 1935-36 he said "The United Kingdom share has increased under almost every item, largely due to the effect

of the differential duties *vis-a-vis* foreign suppliers"[1] As a result of this diversion of trade revenues of the Government of India have also suffered

It was not necessary for India to grant this discriminatory tariff preference to the British steel manufacturers India is the cheapest large-scale producer of pig iron in the world, because she possesses unique natural advantages She has excellent iron-ore deposits, abundant supplies of coal in close proximity, and good supplies of other raw materials like limestone, magnesite and mnaganese Indian pig iron needs no protection and any surplus produced above the requirements of the domestic steel industry can be easily marketed abroad, for it combines to "a singularly successful degree both quality and cheapness" and is much appreciated in the overseas markets

Indian steel industry, however, at present suffers from some disadvantages in comparison with her foreign competitors, due to lack of skilled labour scarcity of technical supervisors, high cost of capital and the necessity of importing plant and machinery Despite these advantages the industry has recorded rapid progress and competes successfully with her foreign rivals The duties imposed on the imports of competitive steel products since 1934 have been more in the nature of anti-dumping provision Therefore, there was no need to resort to discriminatory tariff preference in favour of British manufacturers

Preference within Protection Cotton.—The differential duties were also extended to imports of foreign cotton piece-goods By the Cotton Textile Industry (protection) Act, 1930, the revenue duty on piece-goods was raised from 11 to 15 per cent and in addition, a protective duty of 5 per cent *ad valorem* with a minimum of 3½ annas a pound on 'plain grey goods' was imposed for three years on cotton piece-goods imported from countries other than the United Kingdom. Sir George Schuster justified the exclus on of British goods from the protective import duty

1 Vide p 156.

on the plea that the duty would put a burden on the consumer with a corresponding benefit to the industry[1] In this connnection it is interesting to note that the Government of India, in view of the strong non-official opposition to the principle of Imperial Preference in the Legislature, adopted an extremely unusual and unjustifiable procedure The Legislature was asked to pass the Government proposals without substantial modifications, or the Bill would be withdrawn. Sir George Rainy, the Commerce Member, said, "I would be misleading the House if I conveyed the impression that Government have an open mind, or that they are prepared to discuss these various amendments on the footing that all of these are equally open for consideration. Drastic changes in the scheme embodied in the Bill, it would, I fear, be impossible for the Government to accept"[2] This is a glaring instance of the power of legislative initiative being abused by the Executive, impervious to public opinion The Legislature, therefore, accepted the proposals embodying the differential duties, protection with preference for British goods had to be preferred to no protection at all. This is a mockery of free consent' on which the Majority Report of the Indian Fiscal Commission laid so much stress

The investigation of the Tariff Board on Cotton Industry in 1932 revealed that the extent of British competition in the Indian market was underestimated by Mr Hardy Thus, the very basis on which the imports of British goods were excluded from protective duty was definitely found to be faulty The Board, therefore held that the Indian cotton industry needed adequate protection against the imports from the United Kingdom as well other countries They advanced cogent reasons in support of their findings In the first place, they say that it is extremely difficult to estimate the degree of direct competition from particular countries on the basis of the available data. Even if it were ascertainable with some approach to precision, it would not help to determine separately the extent of pro-

tection necessary against imports from different sources For indirect competition in the form of substitution operated over a wide range of similar, if not identical, articles derived from different countries Secondly, it is as necessary for efficiency and economy to encourage the production in India of goods of finer counts as of medium and coarse counts The Board rightly argued, "If it is granted that there is a case for protecting medium and coarse counts which represent 80 per cent of the aggregate Indian market, then to the extent that the production of finer counts will help to reduce the cost of manufacturing medium and coarse counts in the same mills, the extension of protection to the former must be a logical result of granting protection to the latter, and a necessary step towards shortening the period of protection and reducing the burden on the country"[1] Further, the encouragement of production of finer counts would induce people to grow cotton of superior grades in the country Therefore, the Board recommended uniform minimum specific duties on imports from all countries including those from the United Kingdom These protective duties, uniformly applicable to all imports, the Board did not want to be altered by the Imperial negotiations at Ottawa The Government of India however, it seems, did not approve of the aforesaid proposals, for though the Report of the Board was signed on 10th November, 1932, it was not made public before March 1934 In the meantime, the Indo British Trade Agreement was signed at Ottawa and put into effect Thus, the Government of India ignored the recommendations of the Tariff Board This is not all They signed the Indo-British Trade Agreement at Ottawa in 1932, embodying an extensive scheme of Imperial Preference without any authoritative investigation by the Tariff Board of its economic implications as envisaged by the Fiscal Commission Thus, Imperial Preference became an integral part of our commercial policy without any expert enquiry—nay, inspite of it.

The Indian Tariff (Textile Protection) Amendment Act

1 Vide Report of the Tariff Board on Cotton Industry 1932 p 109

of 1934, incorporating the duties agreed to in the Indo-Japanese Trade Agreement and the Mody-Lees Pact, further, strengthened the scheme of Imperial Preference on cotton piece-goods imported into India. The Tariff Board Report was superseded. The Act, which came into force from 1st May, 1934, goes a step ahead of the Provisions of the Mody-Lees Pact. We will discuss in detail the provisions of the Pact at a later stage. It is sufficient at this stage to note that the Pact provided that in respect of cotton yarn imported from the U.K. the duty be 5 per cent. *ad valorem* with a specific minimum duty of 1¼ annas per pound on all counts be levied. The Act, however, exempted yarns of counts above 50's from specific duties and thus made an important departure from the terms of the Pact.

It seems that the recommendations of the Tariff Board, which were framed with a view to promoting the growth of Indian cotton industry, if adopted by the Government of India, might have affected adversely the Lancashire interests. According to the Report of His Majesty's Trade Commissioner in India the recommendations of the Tariff Board, if adopted, "would have been most damaging to Lancashire interests."[1] He further adds: "The Indo-Japanese Treaty and the Bombay-Lancashire Agreement, by rendering inapplicable the proposals of the Tariff Board, have prevented a further serious blow to our textile trade. The Tariff Board recommended fairly high specific rates on goods from all sources, which would have fallen particularly heavily on the U. K. fabrics. The new Act, by retaining the system of *ad valorem* duties and by making provision for substantial differential margins between the duties on the U. K. and foreign imports respectively, has provided a more equitable basis of fiscal treatment from the U. K. exporters standpoint."[2] *Thus*, the recommendations of the Tariff Board were rejected in the interests of Lancashire. The policy of discriminating protection was once again tempered.

The Indian Tariff (Textile Protection) Amendment Act of 1934 granted protection to the Indian cotton industry for a period of five years, but the duties on British goods were to remain in force only for two years and to be reviewed thereafter by the Tariff Board. Accordingly, a special Tariff Board was appointed by a Resolution, dated 10th September, 1935, of the Commerce Department, Government of India, "to recommend on a review of present conditions and in the light of the experience of the effectiveness of the existing duties, the level of the duties necessary to afford adequate protection to the Indian cotton textile industry against imports from the U.K. of (a) cotton piece-goods, (b) cotton yarn, (c) fabrics of artificial silk and (d) mixture fabrics of cotton and artificial silk." *The term 'adequate protection' was also defined.* According to the Resolution, adequate protection meant "duties which will equate the prices of imported goods to the fair selling prices for similar goods produced in India." The Board was enjoined to give in the course of the enquiry "a full opportunity to the cotton textile industry, whether in India or in the United Kingdom, to present its case and, if necessary, to answer the cases presented by other interested parties." This obligation was imposed in accordance with the terms of the Supplementary Indo-British Trade Agreement. The Board was not required to make any recommendations in respect of revenue duties.[1]

The Board recommended that on bordered grey goods (*i.e., chadars, dhoties, saris and scarves*), bleached goods and coloured goods (excluding prints) the duty necessary to afford adequate protection to the Indian cotton textile industry against imports from the United Kingdom should be 20 per cent. *ad valorem*. On plain grey goods imported from the United Kingdom the Board recommended a duty of 10 per cent. *ad valorem* or 3½ annas per pound whichever

[1] Vide Report pp. 3-4.

CHAPTER XI

INDIAN COMMERCIAL POLICY AND TRADE AGREEMENTS—(Contd.)

Imperial Preference through Indo-British Trade Agreements of 1932—By the Import Duties Act of 1932 Britain had imposed a general duty of 10 per cent *ad valorem* on all imports, with the exception of certain foodstuffs and raw materials The enforcement of these duties on the Indian and Dominion products was, however suspended pending the deliberations of the Ottawa Conference The efforts of the sponsors of the Conference were successful and as a result Indo-British Trade Agreement was signed Under the Agreement, Britain promised to continue to accord free entry to all Indian goods within the scope of the general 10 per cent duty Further, the British Government agreed to impose new or higher duties on certain articles imported into the U K from non-Empire countries A duty of 2s per quarter was imposed on foreign wheat in grain. Foreign rice in husk was charged a duty of 1d per pound Castor oil, linseed oil, coconut oil groundnut oil, rape oil and sesamen oil were subject to an import duty of 15 per cent *ad valorem* Linseed was subject to an import duty of 10 per cent. *ad valorem* Magnesium chloride was to pay 1s per cwt For Empire coffee a preference margin of 9s 4d per cwt was guaranteed To this must be added the assurance given by the British Government under Article 4, not to reduce the margin of preference enjoyed by certain Indian exports in the U K[1] Article 5 of the Agreement laid down that the duty on either wheat in grain or lead would be removed if the Empire producers failed to offer these commodities at world prices and in quantities sufficient to supply the requirements of British

consumers The then existing margin of preference on foreign tobacco was guaranteed for ten years, subject to the condition that the duty on foreign unmanufactured tobacco did not fall below 2s ½d. per pound. In case the duty fell below 2s ½d. per pound, the margin of preference would be equal to the full duty The British Government also agreed to co-operate in any practical scheme that might be agreed between the British and Indian commercial interests for promoting greater use of Indian cotton in the U K.

In return for the foregoing concessions, the Government of India agreed to grant preference on 163 classes of British goods specified in Schedule 'F' of the Agreement The margin of preference was 7½% in the case of motor vehicles and 10 per cent in the case of all other commodities specified in the Schedule It was also laid down that the Government of India would consider, in the light of findings of the Tariff Board, the protective duties to be imposed on goods of cotton and artificial silk according as they are made in the U K. or elsewhere and accord tariff preference of 10 per cent on certain goods specified in Schedule 'G' in case protective duties are not imposed as a result of the recommendations of the Tariff Board.

The agreement was to continue in force until a date six months after notice of renunciation was given by either party If, however, the parties desired any modification in the agreement they were to notify the same and have mutual consultation. In case no agreement was reached within six months of the date of such notice the original party had a right to give another six months to enforce the change desired.

From the foregoing analysis of the Indo-British Trade Agreement it will be seen that the principle of Imperial Preference has become an important feature of our commercial policy The ramifications of such a policy of *de facto* discriminations are apt to be wide It behoves us, therefore to examine whether this Agreement is in the interests of the Indian people who have been made to join

the Empire in the scheme of economic isolation and tariff discriminations[1] It is essential to bear in mind that India is primarily an agricultural country, trying to develop her industries under a policy of discriminating protection This marked characteristic of our economic organisation limits the scope and utility of a policy of de *facto* discrimination or Imperial Preference If India is to develop her industries rapidly and with minimum burden upon the consumers it is essential that the protection should be adequate against all competitive imports irrespective of country of origin The accepted policy of Imperial Preference will impair the effectiveness of discriminating protection *Inadequate protection is a serious danger* As regards the non-competitive industrial imports it is in the interests of the poor Indian consumers that there should be free competition between different suppliers India should be able to get her imports from the cheapest market

Indian exports, consisting as they do, primarily of raw materials and foodstuffs, also stand to lose from this sort of tariff discrimination It is well known that discrimination breeds discrimination India should not be a party to any scheme of this type Under non-discriminatory commercial policy India can successfully sell her agricultural produce If preference becomes a part of Indian commercial policy, foreign countries will, in turn, discriminate against Indian exports by way of retaliation The economic development since the Ottawa Agreements has clearly shown the tendency on the part of non-Empire countries to discriminate against Indian exports of even raw materials and foodstuffs The policy of economic self-sufficiency has come in vogue Synthetic substitutes are being found, which have displaced a number of raw materials This tendency is more marked in Germany and Italy In view of these conditions it is uneconomic for India to continue to be a party to any scheme of preference and strengthen thereby the tendency towards eco-

nomic self-sufficiency If, however, other countries continue to discriminate against Indian exports,—although they would rarely do so,—she can effectively retaliate against them India has little to fear from discrimination practised by other countries, if she is not herself a party to any scheme of preference or other form of discrimination

The most important question that needs to be examined at this stage is the effectiveness of the British threat of tariff discrimination The Report of the Indian Delegation says · "The issue so long debated whether there should be a general scheme of trade preference within the Empire was now settled and the question which those responsible for India's fiscal interests had to face was whether India was justified in maintaining her former attitude of aloofness, whether in fact she could afford to stand out of the agreement which seemed likely to include most, if not all, Empire countries other than herself It was no longer a question of what India stood to gain but what she stood to lose"[1] That India by keeping out of the Imperial economic block would have lost some of the markets cannot be denied But it is equally true that the loss would have been soon recouped The non-Empire markets would have gradually absorbed more of the Indian produce Besides, India's abstention from the scheme of Imperial Preference would have meant a vindication of the principle of sanity in the regulation of international trade and, probably, caused serious damage to the scheme The movement for economic self-sufficiency, which gathered momentum after the Ottawa Agreement, would have received a setback. Above all, it is doubtful whether Britain, in her own interests, would have enforced her threat

The Mody-Lees Pact.—The scheme of Imperial Preference underlying the Indo-British Trade Agreement was strengthened by another agreement between the Indian and British commercial interests It has been shown that under the Indo-British Trade Agreement the British Gov-

ernment had agreed to co-operate in any practical scheme that might be devised by the British and Indian commercial interests for encouraging the consumption of Indian raw cotton by the Lancashire cotton mills The Bombay Millowners, therefore, entered into a commercial agreement with the British Textile Mission The main features of the Agreement were as follows

(i) The parties agreed that the Indian cotton textile industry is entitled, for its progressive development, to a reasonable measure of protection against the imports of British yarns and piecegoods It was also agreed that owing to lower costs and other factors operating in foreign countries, the Indian cotton industry required higher level of protection against them than against the U K

(ii) *As regards cotton piecegoods, it was agreed that if* and when revenue position of the country made it possible for the Government of India to remove the general surcharge on all imports imposed in October 1931, the Indian side would not make fresh proposals with regard to the duties applicable to British imports [1]

(iii) In the case of cotton yarns, the Indian side agreed that the duty on British imports would be 5 per cent *ad valorem* with a minimum specific duty of 1¼ annas per pound

(iv) In respect of artificial piecegoods the Indian side agreed that the duties on British goods would be 30 per cent

(v) In so far as the Empire and other overseas markets for piecegoods and yarns were concerned the parties agreed that any advantages which might be arranged for British goods would be extended to Indian goods, and that India, in markets in which she had no independent quota, would participate in any quota which might be allocated to the U K In respect of overseas markets in which Indian mills lack established connections, it was agreed that the

Manchester Chamber of Commerce would use its good offices to bring about contacts between Indian manufacturers and British commercial houses which were already established in those markets

(vi) In regard to raw cotton, the Indian side strongly emphasised the urgent necessity for further efforts being made in U K to popularise and promote the use of Indian raw material They welcomed the undertaking that the British Textile Mission would be prepared to recommend effective action being taken and keep the Indian side regularly in touch with developments It was further agreed that other avenues of co-operation in this field would be explored in the interests of the Indian cotton grower

(vii) The understanding was limited in its duration to the period ending on 31st December, 1935

The pact is welcome as it marks the dawn of an era of mutual understanding between the commercial interests of these two great countries and helps to allay the feeling of distrust and suspicion Further, it shows that the Government of India is prepared to endorse an agreement which the Indian commercial community may enter into with industrialists in other countries on the basis of reciprocity [1]

But a close scrutiny of the Agreement reveals glaring defects The most obvious defect is that the Agreement was entered into on behalf of the whole country by the Bombay Millowners Association alone without the support of an important section of cotton mill industry located in other centres The statement issued by Messrs Kasturbhai and Khaitan said "The demands of Lancashire have been to reduce the scale of existing import duty against her The effect of lowering of tariff can only be an increase

in exports from that country and decrease of production of piecegoods in India It cannot fail to have far-reaching consequences not only on Indian mills, but indirectly, also on the handloom weaver and the cotton grower "[1] In view of strong opposition from important sections of the industry, it is doubtful whether the Government of India was justified in incorporating lower duties on British goods agreed to between the Lancashire and Bombay cotton mill industry into the Indian Tariff (Textile Protection) Amendment Act of 1934 referred to in the preceding section The recommendations of the Tariff Board which were definitely against preferential tariff in favour of Britain were shelved Nay, the Government of India went a step ahead of the terms of the Agreement and exempted the British yarns of counts above 50's from specific duties This was a dangerous breach into our protectionist policy

Lack of reciprocity is another glaring defect of this Agreement India made substantial tariff reductions For instance, on British artificial silk goods the duties were reduced from 50 per cent *ad valorem* or 4 annas per sq yard to 30 per cent *ad valorem* or 2½ annas per sq yard, and from 35 per cent or 2¼ annas per sq yard to 30 per cent or 2 as per sq yard on mixed fabrics of cotton and artificial silk This was, indeed a substantial concession To this must be added reduction in the duty on British cotton yarn Further, in respect of British cotton piecegoods India agreed not to impose fresh duties after the removal of general surcharge In return for these tangible concessions, which caused marked breaches into the discriminating protectionist tariff, India got the promise from the British Textile Mission to "recommend effective action being taken in popularising and promoting the use of Indian raw cotton and keep the Indian side regularly in touch with developments"

The Supplementary Indo-British Trade Agreement of 1935—The Government of India entered into a supplementary trade agreement with the British Government in

1 Vide, The Indian Textile Journal October 1933 pp 3 4

nised that import duties constitute an indispensable element in the revenues of the Government of India, and hence revenue considerations would be given due weight in fixing levels of import duties

Third Article of the Agreement is very instructive (i) The Government of India agreed to accord protection to such industries only as after due inquiries by the Tariff Board would establish claims thereto in accordance with the policy of discriminating protection laid down in the resolution adopted by the Legislative Assembly in February, 1923, provided that the undertaking would not apply to safeguarding of industries under the Safeguarding Act of 1933 (ii) The Government of India further agreed that the measure of protection to be afforded would be only as much as would equate prices of import goods to fair selling prices of similar goods produced in India, and that, wherever possible, lower rates of duty would be imposed on British goods (iii) The differential margin of duty thus established would not be altered to the detriment of British goods (iv) The undertaking contained in this Article would not prejudice the right of the Government of India in cases in which they find it essential, in the interests of the revenue, to impose an over-riding revenue duty on imported goods higher than the protective duty required.

These are more important features of the Agreement This Agreement marks an important change in the technique of commercial policy In fact, this agreement fetters the fiscal autonomy India is said to be enjoying The Government of India agreed that the protection to be given to an Indian industry would not exceed what might be necessary to equate the prices of imported goods to the fair selling prices of similar goods produced in India This undertaking marks a new departure, for whereas hitherto the principle of fair selling prices was one of the several tests for determining the measure of protection, henceforth it would be the only primary test and guiding star of Indian commercial policy It is essential to remember

that the experience of other countries has proved beyond doubt that the test of fair selling price is very difficult to enforce and results in unfair treatment of the parties To avoid needless complications and ill-feeling this test has to be tempered with several other considerations Therefore, this test, strictly enforced, will cause serious complications in our commercial relations with other countries This is not all The Government of India also agreed to accord lower duties on the imports of British goods The result is that not only the tariff discrimination has become an integral part of the policy of discriminating protection in India but the British manufacturers can claim the preferential treatment as a matter of right No longer it is discretionary with the Government of India to impose differential duties in favour of British goods, it is a legal obligation Further, the differential duties, thus imposed by the Government of India in favour of British goods, "cannot be altered to the detriment of United Kingdom goods" The Government of India, therefore, ceases to be master of its tariff policy Thus, the policy of discriminating protection, as accepted by the Legislature, stands altered in material particulars, to the detriment of the economic interests of the country The greatest surprise is that the Government of India has given these undertakings affecting the most vital interests of the country without reciprocity, the British Government does not give any pledge in respect of its tariff policy affecting Indian trade

The procedure in regard to the grant of substantive protection to Indian industries is also modified Article IV of the Agreement laid down that when the question of the grant of substantive protection to an Indian industry is referred for enquiry to a Tariff Board the Government of India would accord full opportunity to any industry concerned in the United Kingdom to state its case and to answer the cases presented by the other interested parties The Government of India further agreed that, in the event of any radical changes in the conditions affecting protected industries during the currency of the period of protection,

they would on the request of the British Government or of their own motion cause an enquiry to be made as to the appropriateness of duties in force from the point of view of the principle laid down in Article III and that in the course of such enquiry full consideration would be given to any representations put forward by any interested industry in the United Kingdom

It is interesting to note that the British industries have been given the right not merely to state their case before *the Indian Tariff Board* but also *to answer the cases* presented by the Indian industries The right to answer *the cases presented by the Indian industries amounts to* a serious encroachment upon the claims and privileges o the national industries and fetters the discretion of the Government of India The British Government does not give a similar right to either Indian or other foreign industries even to state their case before the Import Duties Advisory Committee much less to answer the cases presented by the British industries. Further the British Government are given the right even during the period of protection to cause an enquiry to be made as to the appropriateness of existing duties if they feel that in view of the economic changes revision is necessary That the tariff should be promptly adjusted to suit radical changes in economic conditions cannot be denied But it is undesirab e and dangerous to give the right to a foreign country to demand such an enquiry at its d scretion Such *a procedure is apt to cause uncertainty and vexation and* retard the pace of industrial development in the country

In return for these valuable concessions the British Government promised to give consideration to the steps that might be taken in co operation with the respective commercial interests to develop the import from India of raw or semi manufactured mater als used in the manufacture of articles of a class which on importation into India are *subject to differential duties Further they promised to* continue to use all possible efforts in co-operation with *the commercial interests to stimulate the consumption of*

Indian cotton in all possible ways including technical research, commercial investigation, market liaison and industrial propaganda They also promised to continue the duty free entry of Indian pig iron into the U K. so long as the differential margin in respect of imports of iron and steel in India by virtue of the Iron and Steel Protection Act of 1934 was not lessened.

The promise to develop the import of raw cotton from India is indefinite and vague Besides, in view of the lower quality of raw cotton grown in India the scope of its consumption in Lancashire is limited It is, therefore, idle to expect that Lancashire mills will use any considerable quantity of Indian raw cotton and give a definite promise to that effect

The promise of duty-free entry of Indian pig iron into the U.K., in return for differential tariff treatment accorded to British imports of steel products into India, is a poor bargain It will be recalled that under the Ottawa Agreement, in return for preference on the British galvanised sheets imported into India, Britain had accorded duty-free entry to Indian pig iron and sheet bars Under the Steel Industry Protection Act of 1934 Indian pig iron alone was accorded free entry in exchange for preference on the British galvanised sheets imported into India The Supplementary Indo-British Trade Agreement secured duty-free entry for Indian pig iron,[1] in exchange for the guarantee not only of preference on the British galvanised sheets, but also of the existing differential duties in favour of the U K in the case of all other iron and steel products The undertaking to maintain the differential margin in favour of British imports of iron and steel products was rather a costly price to pay which India could ill afford.

Thus, the Agreement marks a new departure in our tariff policy There have been important changes in matters of principle The policy of discriminating protection has been substantially modified The *Manchester*

Guardian rightly remarked that ' the importance of the new Agreement lies in the manner in which India has now agreed to adopt certain substantial modifications in the way in which discriminating protection may be applied "[1] And yet Sir Joseph Bhore the then Commerce Member of the Government of India claimed We have done nothing more than crystalise our past fiscal practice and principles which have been accepted and laid down either directly or indirectly by this Legislature This also explains why it was not necessary to consult commercial opinion in this country We have broken no new ground We have ventured upon no new field Had we done so I have no doubt we would have followed the practice initiated by myself of prior consultation with the com mercial and industrial interests concerned' It is difficu t to agree with this interpretation It cannot be denied that *the Government of India had renounced some of the most important rights in favour of the British manufacturers* This must further limit the utility of half hearted and halting policy of discriminating protection In short the Agreement confered solid advantages [3] on British expor ters in return for vague promises to the Indian exporters No wonder therefore that the Assembly rejected the Agreement when it was placed before it for approval [4]

Results of the Indo British Trade Agreement of 1932 — The *repercussions of this scheme of Imperial Preference* on Indo British as well as world trade should be noted in brief for a detailed analysis of the working is beyond the scope of the present chapter The scheme of preference outlined in the Indo British Trade Agreement of 1932 and subsequently developed under the Mody Lees Pact and the

of whatever origin, will be admitted free of customs duty into the U K. This is a very useful part of the agreement

(4) *Further, the British Government* undertakes *to* maintain, until 19th August, 1942, the existing margin of preference on Indian tobacco over foreign tobacco In case, however, the duty falls below 2s ½d per lb the margin of preference shall be equivalent to the full duty They also agree to co-operate in measures taken to facilitate the marketing of Indian tobacco in the U K

(5) Under Article 6, the drawback of duty on groundnut oil is to be abolished and that on linseed oil modified

(6) Under Article 9 the Government of India guarantees certain margin of preference on British goods specified in Schedule IV (a) On drugs and medicines containing spirits, the margin of preference is Rs 4/-per Imperial gallon on untested and Rs 3/- per Imperial gallon on tested goods (b) 10% margin of preference is accorded on cement, chemicals paints, colours and painters' materials, fents, woollen carpets, floor rugs shawls iron or steel hoops and strips, iron or steel, barbed *wire* and *wire rope*, copper wrought and manufactures, domestic refrigerators, sewing and knitting machines, certain electrical instruments apparatus and appliances, wireless reception instruments and apparatus and component parts thereof, cycles, and non-electrical instruments, apparatus and appliances (c) 7½ per cent margin of preference is guaranteed on motor cars, motor cycles, motor omnibuses, motor vans and motor lorries

(7) Article 10 is interesting as it lays down detailed provisions affecting Indian raw cotton and British cotton piecegoods The British Government undertake that they will continue to use all possible efforts in co-operation with commercial interests to stimulate the consumption of Indian cotton in all possible ways, including technical research, *commercial investigation, market liaison and* industrial propaganda They also take note of the desire of Indian cotton growers that as much as possible of their production of short staple varieties of cotton should be absorbed in the U K The fulfilment of these objectives,

however, they add, depends on the continued pursuit by all interests concerned in India of the policy of improving the quality and staple of Indian cotton exported to the U K by all practicable means The utility of the assurance provided under this clause, in the absence of guaranteed purchase, is limited, since the purchases by Britain will depend upon the improvements in future, in the quality and staple of Indian raw cotton The problem of Indian raw cotton, as already referred to, is essentially one of quality The Indian cotton grower and those interested in his welfare must make strenuous efforts to improve the quality of raw cotton or stop cultivating the same The cultivation of short staple cotton of lower quality is one of the greatest drawbacks in our agricultural economy No wonder, therefore that Britain has declined to give any definite undertaking to purchase short staple Indian raw cotton The undertaking contained in this Article is therefore hardly of any material assistance to the Indian cultivator

In exchange, the Government of India agreed to levy a sliding scale of duties on the imports of cotton piecegoods from the U K The "basic rates" provided were $17\frac{1}{2}$ per cent *ad valorem* on printed goods, 15 per cent *ad valorem* or 2 as $7\frac{1}{2}$ pies per lb whichever is higher on grey goods and 15 per cent *ad valorem* on other goods Thus, under the agreement, the scale of duties were reduced by $17\frac{1}{2}$ per cent in the case of printed goods and 5 per cent in the case of grey and other goods If however, in any year the imports of British cotton piecegoods into India amount to 350 m yards or less, the import duties charged shall be lower than even the basic rates by $2\frac{1}{2}$ per cent These reduced rates will continue in force so long as the imports of British cotton piecegoods do not exceed 425 m yards in any year for the puprose of restricting such annual imports to the maximum yardage thus fixed The enhanced duties are to be reduced to the basic rates after the end of any year in which imports from the U K did not exceed 425 m yards

The maximum annual yardage of British cotton piecegoods to be imported into India under the basic rates of duty varies according to the annual offtake of Indian raw cotton by the U K. Britain was expected to import 500,000 bales of Indian raw cotton in 1939, 550 000 bales in 1940, and 600,000 bales in every subsequent year, to be able to import a maximum of 500 m. yards of cotton piecegoods. If there is a deficiency in the offtake of Indian cotton, the British cotton piecegoods actually imported into India will be deemed to have been increased by 25 m. yards for every 50 000 bales of deficiency or for any part thereof The maximum permissible deficiency was 100,000 bales for 1939 and 150,000 bales in any subsequent cotton year But, if the imports of Indian raw cotton into the U K. fell below 400 000 bales in 1939 or 1940 and below 450,000 bales in any subsequent years, the Government of India may increase the basic rates of duties to be levied on the imports of British cotton piecegoods after consultation with the British Government. In case the imports of Indian raw cotton into the U K. in any year exceed 750,000 bales, the import duty on printed cotton piecegoods will be reduced so as not to exceed the duty charged on other varieties of British cotton piecegoods imported into India. If as a result of this reduction in import duty the imports of British printed piecegoods increase the excess up to a quantity of 25 m. yards will not be taken into account in determining the figure either of 425 m. yards or 500 m. yards referred to above.

The Agreement[1] will remain in force until 31st March. 1942, subject to six months notice of termination by either party.

From the foregoing brief analysis of the terms of the Agreement it will be seen that the principle of exclusive discriminatory preferences continues to be an integral part of our commercial policy To this extent the new Agreement shows no clear signs of any advance towards equality

of treatment or radical reductions in the barriers on world trade

It may, however, be noted that there are a few important changes in the detailed provisions In the first place, articles on which preference is granted under the new Agreement are fewer than those under the previous agreements, particularly in the case of British goods imported into India This change may be taken as a step in the direction of lowering trade barriers It should, however, be remembered that profitting from the experience of the working of the previous trade agreements, Britain has now limited the preferences to those commodities in which she has been able to capture valuable share of the Indian market Further, in view of the recent Anglo-American Trade Agreement Britain had to make some important adjustments in her claims of preferential treatment in the Empire markets The changes introduced by the present Agreement are, therefore, determined by the pressure exerted by the United States and Canada, and the experience gathered from the working of the previous agreements The principle of discrimination remains intact The Cotton Article has introduced quota arrangements

The mutual concessions offered may now be briefly reviewed It has already been pointed out that the number of British goods on which preference is accorded in the Indian market has been substantially reduced Under the new agreement Britain claims preference only on those goods which have greater scope in the Indian market With respect to Indian goods on which Britain has granted preference the conditions are entirely different The number continues to be fairly large In this connection, however a few facts must be noted In the first place, the Indian goods on which preference is given in the British market are raw materials and foodstuffs which must be imported at the minimum cost Besides these goods have a relatively freer world market than the manufactured goods in which Britain specialises Secondly, the preferences accorded to the Indian goods are shared by the

Dominions, colonies and other British dependencies These areas are largely agricultural, with the result that in certain articles they offer very stiff competition with Indian goods in the British market Thirdly, in respect of certain articles on which preference has been accorded India cannot take advantage of the preferences This is so in the case of an article like wheat Fourth, there are some articles on which preference extended to India is of limited value due to restriction schemes This is the case with tea When all these facts are taken into account in assessing the value of preferences granted by Britain on the Indian goods their value becomes considerably lower than the statistical indication of exports and imports The articles which are imported free of duty from all countries into the U K must necessarily be excluded in assessing the value of preferences granted on the Indian goods The nature of demand for the Indian and British goods and their supply must also be taken into consideration in determining the *quid pro quo*

The most important innovation is Article 10 of the new agreement affecting raw cotton and piecegoods We have already shown that there has been a consistent move on the part of the Government of India to grant preference for British goods in the Indian market even when the imports compete with the domestic industry The principle of preference within protection has thus become the guiding principle of our commercial policy The pressure exerted by Lancashire in this direction has been very conspicuous Under the new agreement the claims of Lancashire over the Indian market have been further strengthened The Government of India has undertaken to reduce import duties on British cotton piecegoods without any detailed enquiry by the Tariff Board These lower duties are bound to increase the Lancashire imports into India at the cost of the domestic industry and Japan This will mean a substantial handicap to the domestic industry. The most curious thing to note in this connection is that India has been called upon to undergo this sacrifice without adequate compensation

The imports of British cotton piecegoods during the recent years have tended to decline from about 515 m yards in 1934-35 to 267 m. yards in 1937-38 Under the new arrangement, the Government of India agreed to reduce the import duties even lower than the basic rates in order to push up the imports of Lancashire cotton piecegoods to 425 m yards A further increase up to 450 m yards is allowed at the basic rates which are substantially lower than the rates which prevailed before the present agreement In other words, Lancashire is permitted to almost double her exports of cotton piecegoods over that of the year 1937-38 under the stimulus of substantially lower preferential duties, in return for an undertaking to purchase 500,000 bales of Indian raw cotton in 1939, 550,000 bales in 1940 and 600,000 bales in subsequent years When we recall that during 1935-36 and 1936-37 British purchases of Indian raw cotton amounted to about 5½ and 6½ lakhs of bales respectively, the linking of the imports of British cotton piecegoods to the purchase of Indian raw cotton at such a low figure does not provide any material assistance to the Indian cultivator for whose benefit the Government of India claims to have entered into this new agreement The more beneficial course, given the present structure of the agreement, would have been to call upon Lancashire, in return for the definite and immediate[1] tariff concessions, to purchase Indian raw cotton of specified quality to the extent of at least a million bales This must be coupled with an undertaking by the Lancashire cotton industry to increase the consumption of Indian raw cotton gradually in future It should, however, be pointed out that even this arrangement would not provide a permanent solution of the marketing problem of Indian raw cotton The only proper solution is to improve the quality of our cotton or

per cent with a minimum specific duty of 5¼ annas on plain grey goods on the recommendations of an Interim Report of the Tariff Board Due to the depreciation of the Japanese currency imports from that country had flooded the Indian market and at prices that threatened to neutralise the effects of protective duties imposed by the Act of 1930 The Indian cotton industry therefore required additional protection against the cheap Japanese imports But since the Indo Japanese Trade Convention of 1904 did not permit any discrimination against Japan the duties had to be imposed on all non British imports In April 1933 His Majesty s Government gave notice to terminate this Convention The duties on non British piecegoods were further raised in June of the same year to 75 per cent with a minimum duty on plain grey goods of 6¾ annas per pound In retaliation the Japan Cotton Spinners Association declared a boycott of Indian cotton The enforcement of the boycott immediately affected the exports of Indian cotton and negotiations were started for an amicable settlement of the dispute In September 1933 an official Japanese Delegation arrived in India and direct negotiations with the Government of India commenced An arrangement acceptable to both the parties was made in the form of an Indo Japanese Trade Agreement of 1934

The Agreement was composed of two parts the Convention proper and the Protocol attached thereto The Convention laid down the general principles for regulating trade between the two countries The Protocol provided details of the duties to be levied and the quota arrangements Thus the Protocol marked an important departure in Indian commercial policy quotas were for the first time used by the Government of India for regulating trade

The more important features of the Convention may be noted Firs both the contracting parties agreed to accord *recip ocal most favoured nation treatment* *Secondly both* the p rt es agreed that if any tariff modification introduced by one party adversely affected the interests of the other

year exceeded 1,500,000 bales the quantity thus exported in excess of 1,500,000 bales was to be, for the purpose of determining the relevant quota of Japanese piecegoods, added to the quantity of raw cotton exported to Japan in the following cotton year

The Agreement was very well received by the industrialists, agricultural interests and the general public The industrialists felt happy because of the definite limit placed upon the imports of the Japanese cotton piecegoods into India, which were rapidly increasing and threatening the domestic industry The agricultural interests welcomed the Agreement because it provided an assured market for Indian raw cotton The general public, naturally, appreciated the Trade Agreement which removed the commercial deadlock and restored the normal flow of trade But the defects in the Agreement became apparent soon after it was put into force The quota arrangements, as will be seen from the preceding analysis, covered only the cotton piecegoods imported from Japan The result was that Japan increased the exports of artificial silk goods, which were not regulated by the quota system, from 2 4 crores in 1933-34 to 3 7 crores in 1936-37 Similarly, there was a remarkable increase in the imports of Japanese fents from Rs 12 lakhs in 1933-34 to Rs 83 lakhs in 1936-37 The imports of apparel and haberdashery and millinery from Japan also recorded a rapid rise from Rs 47 lakhs in 1933-34 to Rs 73 lakhs in 1936-37 Further, in respect of piecegoods covered by the quota system, the linear yard basis was taken advantage of and cloth of greater width was imported Besides, since the scope of the quota system was limited only to cotton piecegoods the Japanese competition in other goods increased considerably and adversely affected a number of other Indian industries Thus, notwithstanding the quota restrictions the Government of India did not succeed in restricting the unfair Japanese competition with domestic producers and the need for suitable revision was soon felt

Indo-Japanese Trade Agreement of 1937—In view of the defects outlined above, in the informed circles feeling grew

that the agreement should be radically revised Further, the separation of Burma from India necessitated an adjustment in the Protocol to the Trade Agreement Japan had entered into a separate agreement with Burma and agreed to purchase 65 per cent of the exportable surplus of the Burmese cotton crop or 70,000 bales, whichever was less, in exchange for 42 million yards of Japanese cotton piecegoods A new Indo-Japanese Trade Agreement was therefore negotiated The new Trade Agreement, however, does not make any radical departure from the old one, the changes are only in matters of detail (i) The basic quota of Japanese piecegoods to be exported to India is reduced to 283 million yards and is linked with an export of 1 million bales of raw cotton from India to Japan The figure of 283 million yards is arrived at by deducting the Burmese quota of 42 million yards from the original quota of 325 million yards according to the Agreement of 1934 (ii) In case the export of Indian raw cotton exceeds one million bales, the quota of cotton piecegoods is to be increased by 1½ million yards for every 10,000 bales of cotton, provided that the maximum limit of the quota is 358 million yards This is also arrived at by deducting the Burmese quota of 42 million yards from the maximum of 400 million yards fixed in 1934 (iii) In case the quantity of raw cotton exported from India exceeds 1½ million bales in any cotton year, the excess is to be added to the export of the following year to determine the Japanese quota, but this is not to be cumulative (iv) The quota for piecegoods has been classified and apportioned as follows: Plain greys 40 per cent, bordered greys 13 per cent, bleached (white) goods 10 per cent, printed goods 20 per cent and other coloured (dyed or woven) goods 17 per cent (v) A new provision is added for regulating the imports of cotton fents Fents are defined as *bona fide* remnants not exceeding four yards in length These fents are not to be included in the quota for cotton piecegoods to be exported from Japan But the quantity of cotton fents that Japan may export to India in any cotton piecegoods year is limited to 8 95 m yards If in any year

more than this quota is imported, the excess is to be deducted from the quota of the next year, if imports are less, the deficit is to be added to the quota of the next year

The imports of the silk fents and artificial silk goods were not included in the Agreement, though the need for regulating the Japanese competition in these categories has been felt The Government of India have, therefore, prohibited the imports of artificial silk fents and increased the duties on artificial silk fabrics and artificial silk mixture fabrics by an average of one anna per square yard from 1st April, 1937 This will give considerable relief to the indigenous industry

The quota provisions of the Agreement are more advantageous to Japan than to India. It may be noted that the imports of Japanese cotton piecegoods into Burma, as judged from the figures of recent years, amounted to about 70 million yards annually, which were included in the basic quota of the old Protocol. Under the new Agreement, a separate Burmese quota has been fixed at 42 million yards, instead of 70 million yards with the result that India will have to absorb 28 million yards more of the Japanese cotton piecegoods This may be at the cost of the indigenous mill industry Of course the Burmese market will be open for Indian goods, but the Lancashire competition will have to be faced. Further, Britain may conclude a separate trade agreement with Burma and acquire preferential treatment for her goods in the Burmese market

The small industries which have suffered most from the Japanese competition, have been completely ignored. This is a very serious omission It is necessary that these industries should be adequately protected against foreign competition. What is therefore, needed is a broad-based trade agreement with Japan on a basis of reciprocity In view of her strong bargaining position India has no cause to despair in this direction.

Indo-Burmese Trade Agreement.—On the separation of

India from Burma, an Order-in-Council issued by His Majesty came into force and was to remain in force for a period of three years or until twelve months had elapsed from the giving by either the Governor-General of India or the Governor of Burma to terminate the operation thereof, whichever was a longer period According to this Order-in-Council *status quo* was maintained for three years from 1st April 1937 The Burmese Government gave the notice of termination on 31st March, 1940 A new trade agreement had therefore to be negotiated

The main articles exported from India to Burma are cotton piecegoods, cotton twist and yarn, jute manufactures, iron and steel, coal wheat flour, vegetable oils, tobacco fish and onions India supplies a fairly good amount of cotton piecegoods to Burma Of 137 million yards of cotton piecegoods imported into Burma in 1938-39 about 89 m. yards were supplied by India Out of 177 m yards of piecegoods exported by India in 1938-39, Burma took about 89 m yards Further, about 33 per cent of India's export trade in twist and yarn is with Burma As regards gunny bags, India supplies practically the whole of Burma's requirements India supplies about 50 per cent of Burma's requirements of iron and steel In coal, wheat flour, vegetable oils tobacco and onions, India has practically a monopoly in the Burmese market As regards sugar, India supplies only a part of the market, a very large share of the demand being met by the domestic industry The imports from Burma are chiefly rice, kerosene, petroleum, lubricating and mineral oils, teak wood and timber India imports about 50 per cent of the total exports of rice from Burma In 1939-40 India's imports of rice not in husk from Burma were valued at Rs 17 crores Thus India is an important purchaser of Burmese rice And yet India is not dependent on Burma because imports of Burmese rice amount to about 6 per cent of the total Indian production The exports of Burmese kerosene, petroleum and lubricating oils are almost entirely to India Further, India takes about 60 per cent of Burma's exports of wood and timber

The Indo-Burmese Trade Agreement was signed in March, 1941 About 77 articles specified in Burmese Customs Tariff are on the "free list," while on 179 articles Burma concedes preference to goods of Indian origin of not less than 10 per cent compared with Empire products and not less than 15 per cent against non-Empire goods Chief among the "free list" are coal, raw cotton, cotton twist and yarn, gunny bags, pig iron and certain classes of machinery Chief among the goods which become dutiable at 10 per cent for the first time are certain types of cotton fabrics, raw silk, jute, cement, molasses, condensed milk, aluminium and vegetables Indian tea becomes subject to a duty of two annas per pound, while colonial tea pays three annas Indian chemicals are now dutiable at five per cent which represents a margin of preference of 15 per cent on Empire chemicals Sugar is taxable at Rs 3/- per cwt while on salt, matches and silver bullion the duty will be equal to the excise duty India has also given valuable concessions

The Agreement taken as a whole, confers valuable mutual advantages, though certain sections of the Indian business community may have cause to demur due to imposition of import duties on goods imported into Burma These import duties will materially help to solve Burma's financial difficulties These duties are expected to yield an annual revenue of Rs 1,00,00 000 Relatively moderate revenue tariff imposed by Burma on Indian goods will help them to maintain the present predominant position they hold in Burma market There is a great need of mutual understanding between India and Burma and a willingness to co-operate in solving economic problems We are, in fact, one people, though now practically separated Mutual estrangement should be avoided at all cost

National Commercial Policy for India—From the foregoing analysis it will be seen that the Indian commercial policy is not in keeping with the economic requirements of the country The defects become more glaring when we compare our policy with that of other advanced indus-

trialised countries It has already been shown that almost all countries are seized by a wave of economic self-sufficiency and the sole object they seem to have in view is to restrict the imports effectively so as to protect their own national interests To achieve this aim, extensive and far-reaching measures are being adopted regardless of treaty obligations The most significant feature to note is that even the most advanced industrial countries have resorted to agricultural protectionism of extreme type At the same time all these countries have adopted ingenious devices to push their own goods in foreign markets These remarkable changes in the technique of modern commercial policy have profoundly affected our trade and industries

India should therefore promptly make suitable changes in her commercial policy lest our entire economic organisation get devitalised The policy of discriminating protection in its working, has been found to be half-hearted and halting It needs radical revision The tariff policy of the future should be one of discriminating protection free from the shackles of rigid and narrow limitations as at present in force Today an industry is denied protection if it does not possess an adequate supply of efficient labour—for there is no dearth of inefficient labour —or a large home market, or some of the raw materials In no other country is the tariff policy hedged with such rigid conditions The rigidity of these conditions must be relaxed For instance, it should be sufficient for our purpose if within a reasonable time labour force can be properly trained or there is reasonable home market for the protected industry, surplus outlet to be marketed in foreign countries with the aid of commercial treaties *Likewise, an undue emphasis on an abundant supply of* raw materials is needless and harmful to the economic interests of the country What is most important is that an industry seeking protection must usually be able to

dispense with protection within reasonable time.[1]

Thus freed from the rigidity of these conditions, the policy of discriminating protection should be worked with the aid of a permanent Tariff Board, composed of competent economists, businessmen and lawyers, having no personal interest in any industrial enterprise, with power to call for information To such a Tariff Board, the industries should have a right to refer their claims for investigation, without the intervention of the Commerce Department and the Board be free from the restrictions imposed by the terms of reference laid down by the Executive The Board should have power to make full enquiry affecting an industry claiming protection The report of the Tariff Board should be promptly published and its recommendations in the form of a Bill be placed before the Legislature Further, the Tariff Board ought to be empowered to supervise the entire commercial policy of the country It should suggest the form and general contents of commercial treaties India may enter into with other countries

As regards the nature and form of commercial treaties, our future policy should be two-fold, long-term and immediate Our long term policy will have to be based on the unconditional reciprocal most-favoured-nation treatment, and minimum trade barriers consistent with reasonable economic requirements of the country In the immediate future, however, our task should be to promote rapid

internal industrial development as determined by the policy of discriminating protection discussed above, and at the same time safeguard our trade and industries against the danger of quotas, exchange control, clearing agreements, bilateral trade pacts, tariff barriers, etc. Our commercial policy, therefore, must take into account all recent changes in the technique of protection, protect our economic system from their adverse effects and help to reduce the growing trade barriers on international trade It should promote fuller national economic development and help to improve international economic relations Our commercial treaties, in view of the present world economic conditions, will be bilateral in form but multilateral in character India will extend full co-operation to all those countries willing to adopt liberal commercial policy To achieve this objective, India will have to enter into broad-based commercial treaties with important countries and take effective measures against those which refuse to reduce their restrictions on Indian goods. Moderate tariff and other trade barriers. determined by the reasonable economic requirements of the contracting parties, would be given due consideration Such a policy would give full scope for the economic development of the countries concerned and promote most efficient and effective utilisation of world's economic resources. The narrow bilateral pacts, like the Indo-Japanese Trade Agreement, or trade agreement based on exclusive tariff preferences, like the Indo-British Trade Agreement, are not desirable

Needless to add that there is no scope for Imperial Preference in the Indian commercial policy Since the Indian tariff policy will be in keeping with her reasonable economic requirements there will be no room for preference The foreign countries should have no cause to demur since all those following liberal commercial policy will be allowed equal opportunities in the Indian market What India needs is a scientific and effective national commercial policy to promote the most efficient utilisation of her economic resources

We may now summarise our conclusions

(i) The policy of discriminating protection followed by the Government of India has rendered invaluable assistance in promoting industrialisation but the progress has been *slow due to the rigid conditions that have been imposed* and the most obvious defects in the procedure adopted Suitable modifications ought to be effected to make the policy more effective and prompt

(ii) The traditional policy of *laissez faire* followed by the Government of India till 1923 has retarded the economic development of our country

(iii) There is no room for Imperial Preference in Indian tariff policy

(iv) Narrow or exclusive preferential bilateral trade agreements will scarcely serve any useful purpose

(v) India should enter into broad based trade agreements and the concessions may be shared by all those countries which undertake to follow liberal tariff policy consistent with their reasonable national economic requirements

CHAPTER XII

FUTURE COMMERCIAL POLICY

Reasonable Protection is Essential for Backward Countries.—The detailed analysis of the technique of commercial policy given in the preceding chapters has brought to striking relief its defects and the serious repercussions on the volume of world trade and the economic well-being of the general mass of the people throughout the world. The volume of world trade has declined considerably, which has led to unemployment and a substantial fall in the standard of living of the people. The growth of economic autarky has led to a colossal waste of economic resources. These dangerous trends must be checked to safeguard the economic future of the world. In short, the technique of modern commercial policy must be suitably modified to secure an expansion of international trade and the most efficient utilisation of the economic resources of the world. In the present chapter, therefore, we shall state our positive proposals of policy.

The commercial policy of the future must recognise reasonable national economic requirements of the people of a country if it is to promote efficient and effective utilisation of the economic resources of the world. The history of modern economic development shows that most of the advanced countries, in attempts to reorganise the structure of their industries from small-scale to mass production on a factory basis, have had to resort to protection for safeguarding their industries against the unfair competition of more efficiently organised foreign rivals. In the first chapter we have shown that the United Kingdom, Germany, France and the United States of America[1] organised their industries with the aid of protection. Their

against a commercial policy It would promote the most efficient utilisation of world economic resources International trade would then be based on the principle of complementary exchange, comparative costs would determine the channels of trade

Protectionist policy has its dangers In practice, protection has often been continued, due to the vested interests created thereby, even after the industries have grown to full maturity, at a tremendous cost to the taxpayer In other words, protection has tended to perpetuate itself. Cases are not lacking when protection has bred inefficiency, due either to an over-dose of protection or lack of adequate and effective supervision over the industries receiving state assistance To achieve its objective, a national scheme of protection must be very carefully thought out and strictly enforced There should be a permanent economic authority to keep a careful and continued watch over the working of the entire policy of protection The cost of this scheme to the taxpayer should the minimum compatible with maximum efficiency Economy and efficiency should be the watchword of this national policy of protection Thus, the state has a great responsibility cast upon it both in formulating and working the scheme of protection, so that the waste of national economic resources and causes of international friction may be minimised The task is obviously very delicate and difficult Yet, there is no cause for pessimism or despair A well-informed public opinion would make the task much easier and responsible public criticism be an invaluable guide The public should therefore be taken into confidence and kept well-informed

Tariffs —The technique of modern commercial policy analysed in the preceding chapters can hardly stand this test The tremendous rise in tariff levels, particularly since the depression, cannot be said to be determined by the reasonable economic requirements of the countries imposing them The Hawley-Smoot Tariff Act and the retaliation by foreign countries which followed thereafter were dictated by the vested interests, out for exploiting political

and other sentiments for sectional ends Imports were restricted and inefficient enterprises propped up within the national boundaries, which raised the cost of living of the people and created international friction The Governments of the countries concerned could resort to these misguided and wasteful devices because they did not take into confidence the general public opinion in formulating their policies In fact, attempts have been made, even in democratic countries, to evade public criticism by restoring to new devices for regulating trade For instance, quotas, as an instrument of commercial policy, vest the power largely in the hands of the executive, which can restrict trade more effectively without any interference from the legislature The power of the legislature is considerably reduced in determining the details of commercial policy Further, the dangerous effects of quotas on the economic welfare of the people are largely concealed so that the public cannot readily understand their implications The result is that public criticism of these restrictive commercial policies is much less vigorous In the case of exchange control, the working of the entire machinery is kept as a closely guarded secret For instance, the working of the Exchange Equalisation Account in England is an *official secret The public gets to know the details of its* working when they cease to have much practical value Thus, it is clear that the Governments are afraid of well-informed public criticism because their restrictionist commercial polices are not in the national interests The general consensus of economic opinion demands the creation of conditions which would permit maximum trade expansion. The obstacles to the growth of international trade should be removed In this crusade for a more liberal commercial policy a frontal attack must be made on the general tariff level Tariffs must be substantially reduced

The lead in the reduction of tariffs must come from advanced industrialised countries like the United Kingdom, the United States of America and France The trade agreements programme of the United States has made a distinct contribution in this direction, though its effectiveness has

been limited by the restrictions imposed upon the powers of the President and the lack of sufficient response from other advanced countries In this respect, Great Britain, being one of the most advanced industrialised countries, is most to blame. Her policy as described above, has spurred the sentiment of economic self-sufficiency and caused irreparable damage to international economic relations The British agricultural policy and the vigorous drive for exclusive imperial preference[1] are significant in this connection Even today there is no indication on the part of the British Government to give up either the policy of de *facto* discrimination or of agricultural protectionism. The Anglo-American trade agreement has, undoubtedly, helped to reduce the height of preferential tariff within the British Empire But, it does not go far enough, the dangerous principle of commercial discrimination has not been seriously assailed The British policy of bilateral trade agreements is not sufficiently reassuring The French commercial policy is no better The totalitarian states are not free from blame for the present chaos in which we find ourselves It is essential that both Britain and France should sincerely and earnestly co-operate with the United States in reducing trade barriers Success in lowering the trade barriers can be achieved only if all these three advanced countries are prepared to discard the de *facto* discrimination implied in the policy of Imperial Preference,[2] reduce protection to the limits determined by their reasonable economic requirements, and adopt the un-

conditional Most-Favoured-Nation Clause in their bilateral trade agreements, which would thereby become multilateral in character though bilateral in form Another essential condition for the success of this new commercial policy is that only those countries which are prepared to mould their commercial policy on these lines should be permitted to enjoy the benefit of concessions through the operation of the Most-Favoured-Nation Clause in their trade agreements If this condition is not observed with scrupulous care there would be no incentive for lowering tariffs or other trade barriers This would no doubt mean an immediate substantial sacrifice of the sectional interests on the part of the countries giving the lead [1] but the gains accruing from this liberal policy would soon multiply and more than repay the parties

Quotas.—A more serious menace to the growth of international trade comes from the extensive use of the import quotas In chapter four it has been shown that since the depression the use of import quotas as an effective instrument of commercial policy has increased considerably Import quotas are more quick and certain in their effects than the customs duties They have considerable administrative advantage over tariffs In the case of national emergency, which demands a drastic cut in the imports, quotas can be effectively utilised But, it is this efficiency of the quota system, in effectively excluding the imports which constituted a more serious menace to the normal flow of international trade The executive is apt to make use of it for concealing the defects of its economic policy and to escape public criticism The import quotas, if they are to serve national economic requirements ought to be cautiously and sparingly used, in the case of emergency alone It is a very dangerous instrument of commercial policy, it distorts the entire mechanism of exchange The quotas, being rigidly and arbitrarily fixed, obstruct, more effectively than tariffs any automatic adjustment of inter-

national trade to the changes in the economic structures of the countries adopting them. Besides, the quotas, since they do not fall within the purview of the Most-Favoured-Nation Clause, have led to unlimited discrimination, caused retaliation and strangled world trade. To combat the formidable obstacles to trade created by the use of import quotas by one country others are also led to resort to similar tactics. The evil is contagious.

No wonder, therefore, that the plea that the import quotas should be abolished as early as possible has received wide recognition. The Report of the Export Committee on International Economic Reconstruction, appointed by the International Chamber of Commerce, recommended that the quotas should wherever possible be immediately abolished. In other cases similar measures should be taken "at a not too distant date." To achieve this objective the Committee recommended that the states should subscribe to multilateral agreement on the necessity of abolishing the quota system, and replace the existing import quotas by tariff quotas during the period of transition. They felt that industrial quotas are easier to remove than agricultural quotas, and therefore recommended that serious efforts should be made to remove all industrial quotas within two years of the issue of a multilateral declaration to that effect. Where, however, the import quota system cannot be immediately suppressed their general working should be improved. M. Van Zeeland offered similar suggestions. He recommended the gradual suppression of all quotas on industrial goods, and their replacement, if necessary, by ordinary import duties or by tariff quotas. He, too, recognised that there are special difficulties in the way of removing agricultural quotas, and, therefore, suggested that countries should enter into an agreement not to impose new agricultural quotas or to tighten up the existing ones.

It is difficult to secure any substantial success in suppressing the import quota system unless the advanced countries are ready to renounce their ultra-protectionist policies. What is needed is a bold, courageous and sincere

lead from the advanced countries, who need least the aid of protection for their ordered economic development. If these countries snow their willingness to limit their schemes of protection in accord with their reasonable economic requirements, and make a joint declaration to that effect it would immensely facilitate the general removal of trade barriers It is not intended to convey that these leading countries should themselves immediately and suddenly remove all import quotas or other trade barriers to set an example for other countries to follow Far from it Such a sudden and hasty action would dislocate the entire economic system of the countries concerned and have an undesirable effect upon other countries as well What is needed of these countries is the declaration of an honest and sincere intention to play the part, determined by their economic position, in international economic reconstruction This is an essential pre-requisite of any future scheme of economic reconstruction

Further any scheme of international economic reconstruction even in its initial stages, must cover both industrial as well as agricultural quotas A clear cut demarcation between the two is difficult to maintain and would undoubtedly endanger the success of the scheme In this connection the remarks of the Expert Committee are significant They said "Economic self-sufficiency in agricultural commodities is an ideal which is of more than economic significance Moreover the demand for agricultural products is much more inelastic than the demand for industrial products It is therefore not easy to envisage a time in the near future when the complete abolition of agricultural quotas would be possible by international agreement"[1]

Relatively greater reluctance on the part of advanced industrialised countries to discard their agricultural quotas on non-economic grounds, on which the fears of the Committee are based, cannot provide the necessary atmosphere for the suppression of quotas or other trade barriers Per

contra, it strengthens the case of autarky. The relatively backward industrialised countries would, naturally, be more reluctant to give up the industrial quotas, and would be forced to start a more vigorous drive for rapid industrialisation for the utilisation of their agricultural products which fail to find export markets It is essential, therefore, that the quota system as a whole should be assailed Piece-meal efforts are bound to fail

To start with, the administration of the import quota system should be improved This should not be very difficult to achieve since it would cause least disturbance to the industrial structure of the countries using them. Per contra, the improvement in administration would bring about substantial saving in both time and money

After improving the administrative machinery, attempts should be made to minimise the discrimination implicit in the import quota system. The quotas should be distributed on an equitable basis amongst the importers Such a measure would not call for any sacrifice on the part of the country which makes use of the quotas for helping its domestic industries and trade

Further, the import quotas, being more effective than tariffs in checking imports, should be fixed very carefully, after a thorough investigation by an expert committee of the national needs and the economic implications of the new measure proposed to be undertaken The import quotas should not be arbitrarily fixed as hitherto The unlimited discretion of the executive should be carefully fettered, without impairing the efficiency of the system. An over dose of protection, which an arbitrary quota implies, is both costly and dangerous

The next step in the direction of the suppression of the import quota system should be the agreement not to impose new quotas or to further tighten up the existing ones This undertaking should be incorporated in the bilateral trade agreements containing the Most-Favoured-Nation Clause Thereafter the quota restrictions should be gradu-

ally relaxed and replaced by tariffs The process of relaxation must be gradual so as to avoid any dislocation in the economic structure of the countries affected thereby.

Exchange Control—Exchange and clearing agreements, as has been shown in the preceding chapters, are very serious obstacles to the growth of international trade To restore the normal functioning of the international economic mechanism, those formidable barriers should be removed at the earliest opportunity Any step that may be taken in this direction should, however, be very carefully thought out In view of the present international economic conditions, the parties would be reluctant to give up these measures unless they are assured that the change over would cause no serious strain The change should, therefore, be gradual

Sudden and violent changes in the rates of exchange between national currencies must be checked to minimise the speculative movements of short-term funds and reduce the uncertainty to industrialists and businessmen It is agreed that international trade must suffer so long as the rates of exchange are highly unstable The adjustment of the rates of exchange at a level determined by the internal economic structure and the international markets is an essential pre-requisite of any scheme of exchange stabilisation There is a marked disparity between the national and international cost and price structures The rates of exchange should permit the adjustment of balance of payments and free functioning of the economic system Variations in the rates of exchange should not be used as an expedient for artificially pushing exports This would secure much needed relative stability Fortunately, the trade agreements negotiated by some of the important countries, as noted above, contain definite provisions against undesirable variations in rates of exchange This tendency should be encouraged and strengthened With the return of normal international economic conditions a more permanent stabilisation should be promptly attempted

Restrictions on the transfer of funds from one country

to another present a more serious obstacle to the movement of international trade than exchange fluctuations During the depression exchange control was adopted by several countries to meet the strain on balance of payments, caused by the cessation of the flow of new foreign loans, recall of old loans, the flight of domestic funds and the continuous fall in their exports It is evident, therefore, that the measures of exchange control can be removed only if the forces which are responsible for their present extensive use are promptly and effectively checked The first step in this direction is not merely to stop the abnormal and embarrassing flow of funds to the major countries but to reverse it This would be beneficial both to the creditor as well as debtor countries The creditor countries would profit from this measure because it would stop an upward pressure upon their currencies from heavy and prolonged influx of capital In the United Kingdom and the United States the influx of "hot money" has presented serious problems and Exchange Funds have been used to protect the internal economic structure from inflationary effects The Exchange Funds are, however, mere palliatives The real problem is one of maldistribution of capital which must be seriously tackled The flight of capital can be checked by restoring financial stability

For restoring financial stability the resumption of international lending is essential Loans must be advanced for stabilising the currencies of the weaker countries and for meeting their financial requirements This would engender confidence in the business community and help thereby the growth of international trade

Short-term loans should be advanced more frequently to finance the imports of debtor countries, who have been disabled to pay off their past debts This would enable the creditor countries to widen the markets for their goods, and at the same time accord an invaluable assistance to the debtors in meeting their essential economic requirements more adequately. In recent years some of the business bouses have taken a more practical attitude and

advanced credits for financing current transactions irrespective of the past unliquidated debts What is needed is that the Governments of the creditor countries should encourage and aid such transactions.

Long term loans will have to be advanced for financing the capital development of backward debtor countries Of course to permit the transfer of capital from the lending to the borrowing countries the latter will have to remove their import restrictions These loans will enable the creditor countries to increase the export of their capital good The debtor countries will be able to extend the scope of their economic activities with the help of capital equipment thus acquired The purchasing power of the people in the debtor countries and the ability of their Governments to pay off the debts would automatically increase as a result of added efficiency in the technique of production and relative exchange stability Improvement in the economic conditions of the debtor countries is an essential condition precedent to the removal of exchange control and the development of world trade

As regards the past indebtedness it should be carefully studied and scaled down by mutual agreement wherever necessary The sums thus agreed to may be consolidated, interest rates thereon reduced in keeping with the market conditions and the payments spread over a fairly long period so as to avoid any dislocation in the economic structure of the debtor countries Above all the creditor countries will have to remove the high tariff and other import restrictions so as to permit the debtor countries to pay off their debts in goods and services The creditor countries will have to admit larger imports In this connection the change in the American commercial policy discussed above is welcome and augurs well for the future of world commercial policy

The Most Favoured Nation Clause—The essential condition for the most efficient and effective utilisation of world s economic resources and the growth of international trade is equality of treatment Discrimination breeds

inefficiency and leads to retaliation The trade agreements should, therefore, be so framed as to secure equality of treatment The M F N Clause in its unconditional form, if included in the commercial treaties, provides the best available guarantee of equality of treatment The abuse of the Clause should however, be carefully guarded against The countries following restrictionist commercial policy should be debarred from sharing the benefits accruing under the Clause The spirit of the M F N Clause should guide the commercial policy of the future rather than merely the letter The countries claiming to share the benefits under the Clause should be compelled to respect the obligations arising therefrom The scope of the Clause should be widened so as to include all forms of commercial discrimination Under the present abnormal economic, conditions, with excessive trade barriers and autarky in vogue, adequate support to the M F N Clause may not be, probably, forthcoming Here, too, much depends upon the attitude of the advanced industrialised countries Great Britain, United States and France can do a great deal in removing discrimination and restoring equality of treatment in commercial practice, on which the future of world trade essentially depends The present chaotic condition of commercial policy is in no way due to any defects in the M F N Clause, as is not unoften made out The defect lies in the narrow and rigid interpretation put upon the Clause in order to escape its obligations If the Clause is liberally interpreted and scrupulously enforced it would be invaluable both in reducing the trade barriers and in providing the equality of treatment Prof Viner rightly points out that the most-favoured-nation pledge should not, or need not, be granted as a routine matter, and as merely an incidental provision in stereotyped treaties of commerce and navigation It should, instead, be made an integral part of tariff treaties, and accorded, reciprocally, as one of the significant items in the mutual exchange of considerations. The life of the pledge, moreover, should be made coterminus with the life of the other provisions in the tariff treaty. To countries

with low-tariffs and non-bargaining policies most-favoured-nation treatment should be extended without a pledge, or if such a pledge is incorporated it should be subject to termination in case of departure from the low-tariff policy by the countries receiving the pledge High tariff countries which refuse to engage in tariff-reducing negotiations should not be given a pledge of unconditional most-favoured-nation treatment, and whether in practice such treatment should be extended to any of these countries or withheld from them should be determined as expediency may dictate [1]

Bilateral Trade Agreements—Under the present world economic conditions, bilateral trade agreements containing the unconditional M F N Clause would be more effective in reducing trade barriers than the multilateral agreements [2] The recent experience of multilateral agreements[3] is not at all encouraging At best, a multilateral agree-

ment would provide for an uniform percentage reduction in the general level of tariffs of the signatory countries Such a horizontal cut must be inequitous and essentially conservative An uniform cut applicable to all the participating countries would be inequitable because the incidence of tariffs cannot be precisely determined by comparing the absolute levels of a group of countries The scope of such agreed reductions is apt to be limited. The maximum reduction that can be expected under such an agreement is 10 to 15 per cent But, in view of the tremendous increase in the height of tariffs since the depression, such conservative cuts will not suffice What is needed is a more vigorous drive for the reduction of tariffs as well as other forms of trade barriers Bilateral trade agreements, containing the unconditional Most-Favoured-Nation Clause would secure larger reductions The recent experience of the United States in this direction is sufficiently encouraging This policy should be strengthened. The future of commercial policy rests essentially on mutual understanding between nations

Proposed Commercial Policy for India · A Contribution to Economic Reconstruction.—A word about India may be added. Indian commercial policy should be suitably modified to bring it in line with the above proposals Being an industrially backward country, with ample natural resources awaiting fuller utilisation, India should adopt a policy of protection and apply it with "discrimination," in keeping with her reasonable economic requirements The tests of "discrimination" at present in force should either be relaxed or liberally interpreted The protective tariff thus determined, should be adequate and secure equality of treatment.[1] This should be the minimum tariff The protectionist policy must be administered with the assistance of a competent and permanent Tariff Board, to minimise waste of economic resources The experience of the working of tariff boards in Canada and Australia will

be an invaluable guide in this direction Protection should be essentially temporary The interests of the public would be safe in the bands of an impartial, competent and permanent Tariff Board

Preference within protection is dangerous and undesirable This is not all India need not complicate her commercial policy by resorting to discrimination in the form of Imperial Preference It has been shown that this form of discrimination has played an important part in strengthening the trend towards autarky Besides, India has not derived any material benefit from the scheme of Imperial Preference In future, too, India would not profit from this sort of discrimination, in view of the structure of her trade and industries If India, therefore, discards Imperial Preference from her commercial policy, she would promote her economic interests and at the same time make a valuable contribution towards economic reconstruction

India's experience of quota system is not very encouraging Therefore, the use of quotas, in future, should be discouraged This change in Indian commercial policy would be materially useful in the reduction of trade barriers

With moderate protectionist tariff, determined by her reasonable requirements, India should enter into broad-based commercial treaties,[1] containing the unconditional M F N Clause, with foreign countries and permit full scope to their goods in the Indian market on the condition that similar facilities are extended to Indian goods in their markets Discrimination should be entirely removed from Indian commercial policy The tenure of the treaties should not be less than seven years Period of three years, as adopted by the United States, is rather short for industrial stability Such a policy would help to lower trade barriers, for the countries refusing to follow liberal commercial policy would be penalised With the countries

which propose to continue restrictionist policy, India may have temporarily to resort to narrow commercial bargaining as an expedient to tide over the emergency But such countries would be denied unconditional most favoured-nation treatment, so long as they continue to follow the restrictionist commercial policy This black listing would have sufficiently deterrent effect on these countries to give up their restrictionist policy and adopt a more liberal attitude The experience of the United States since 1934 is very helpful in this direction If Indian commercial policy is moulded on these lines, India would be able to play an important part in the reduction of trade barriers and improvement of international economic relations

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